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Germany's surprising economy

Aug 20th 2005

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Politics this week

Aug 18th 2005
From The Economist print edition

AP

Leaving Gaza

Israel began the withdrawal from all 21 of its settlements in the **Gaza strip**. After a two-day grace period, Israeli troops moved in to evict hundreds who did not want to leave voluntarily. Separately, a settler in the northern West Bank shot dead four Palestinians. Israel's prime minister, Ariel Sharon, called the incident a “Jewish terror act”.

See article

The deadline was extended for negotiators to agree a new constitution for **Iraq**. Having failed to settle their differences by August 15th, they were given a new target of August 22nd. Sticking points remain on the issues of federalism and the role of Islam. Two days after the original deadline expired, three car bombs in **Baghdad** killed at least 43 people. One of the bombs was detonated near a hospital as some of the wounded were arriving for treatment.

See article

The International Monetary Fund reported that **Iraq's economy** grew by about 50% last year, fuelled by a recovery in oil production. But the economy remains “fragile”, with “daunting challenges” ahead.

See article

There seemed to be no concessions to the reformist wing of **Iranian politics** in the newly elected president's choice of key cabinet ministers. Mahmoud Ahmadinejad nominated known hardliners to the foreign, intelligence and interior ministries.

See article

Zimbabwe's government resorted to desperate measures to try to stop the country going broke. Herbert Murerwa, the finance minister, announced sweeping tax rises, including a rise in VAT from 2.5% to 17.5% that he hopes will raise 6.6 trillion Zimbabwean dollars (around $146m at black-market rates).

Pushing the limits

The assassination of Lakshman Kadirgamar, **Sri Lanka's** foreign minister, raised fears that a tenuous ceasefire in force since 2002 might break down entirely.

See article

Around 350 small homemade bombs were detonated across **Bangladesh** within an hour of each other, killing two people and injuring over 100. Suspicion for the attacks fell on an Islamic group that the government banned in February.

Indonesia's government and the GAM rebels in the western province of Aceh signed a peace agreement. In return for ending their war, the rebels get autonomy for their province and an amnesty, but not independence.

See article

Russia and **China** began eight days of joint military exercises—their first ever—to practise combating “international terrorism, extremism and separatism”. Russia is also keen to sell China more weaponry.

Singapore hosted a 13-nation exercise in the South China Sea to practise stopping vessels suspected of carrying weapons of mass destruction under the American-sponsored **proliferation security initiative**.

Choking smog from forest fires in Sumatra enveloped Kuala Lumpur and other **Malaysian** cities. The prime minister, Abdullah Badawi, told people to pray for rain.

A broader dispute

Arizona declared a "state of emergency" along its border with Mexico in order to boost funds for local enforcement efforts. Governor Janet Napolitano criticised the federal government for not doing enough to stop a recent surge in illegal immigration and drug-smuggling there. **New Mexico** declared a similar emergency in four border counties last week.

California's governor, Arnold Schwarzenegger, received a fillip to his reform plans when the state's Supreme Court ruled that his measure to allow the redrawing of notoriously gerrymandered electoral boundaries can appear on the ballot in November.

Amid growing problems for the Republicans in **Ohio**, the state's governor, Bob Taft, was charged with failing to report dozens of gifts bought for him by supporters.

A judge delayed the implementation of a new pay and personnel system for federal workers at the **Department of Homeland Security**, which was due to start on August 15th, ruling that it didn't provide for collective bargaining rights. The Bush administration argues that it needs greater flexibility at the DHS for national-security reasons.

Frightening tales

Two successive **aeroplane crashes** unnerved travellers. Over 120 people died when a Cypriot plane that had lost cabin pressure hit a Greek mountain. Two days later, 152 passengers from **Martinique**, a French overseas territory, died when a jet belonging to West Caribbean, a troubled Colombian airline, crashed in northern Venezuela.

Angela Merkel, the centre-right opposition candidate for chancellor in Germany, picked a "shadow cabinet", including a radical tax reformer, Paul Kirchhof, as potential finance minister. The lead of Ms Merkel's party over Chancellor Gerhard Schröder's party continues to shrink ahead of the election, due on September 18th.

See article

Bulgaria at last has a government, over a month after its election on June 25th. The outgoing prime minister (and ex-king), Simeon Saxe-Coburg, whose centrist party lost, agreed to serve under the socialists in a grand coalition.

Too late for contrition?

AP

Brazil's president Luiz Inácio Lula da Silva went on television to apologise for his party's role in a corruption scandal, but denied any personal knowledge of irregular payments. His publicist told a congressional committee that he was paid $3.25m from an offshore slush fund for his work in the 2002 election campaign.

See article

At least 35 prisoners died in **Guatemala** after battles broke out between members of two rival gangs in several of the country's jails. The inmates were said to be armed with grenades and machineguns.

More than 100 **Ecuadoreans** trying to emigrate to the United States drowned when their boat, designed to hold 15 people, sank off Colombia.

Peru's finance minister, Pedro Pablo Kuczynski, took over as the country's prime minister. His

predecessor resigned after President Alejandro Toledo tried to appoint Fernando Olivera, an unpopular ally, as foreign minister.

See article

Cuba's Communist government celebrated the 79th birthday of Fidel Castro. Mr Castro remains in active charge, despite breaking his knee and arm last year.

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Business this week

Aug 18th 2005
From The Economist print edition

Icahn's latest prey

Carl Icahn, a billionaire investor, revealed that he and three partners now control 2.6% of shares in **Time Warner**. Mr Icahn is using the stake to persuade other shareholders to join him in pressing the media conglomerate to shed its cable-TV unit and to buy back $20 billion in shares in order to boost its share price.

See article

Commerzbank confirmed that its chief executive, Klaus-Peter Müller, is being investigated by German authorities as part of a money-laundering inquiry involving a Russian telecoms firm during the 1990s, when Mr Müller was head of the German bank's east European operations. Commerzbank's management board said that Mr Müller will be “completely exonerated”.

Germany's financial regulator, BaFin, has opened a formal inquiry into possible insider trading in shares of **DaimlerChrysler**. The watchdog is concerned about transactions conducted shortly before Jürgen Schrempp unveiled his intention last month to step down as the carmaker's boss.

John Mack, the new chief executive of **Morgan Stanley**, decided not to sell the Wall Street firm's Discover credit-card business. His predecessor, Philip Purcell, had said he would spin the unit off just before he was ousted in June. Morgan Stanley also said it would sell its aircraft-leasing business and appointed three new directors.

Bank of China, one of China's four big state-owned banks, said a group of foreign investors led by **Royal Bank of Scotland** will pay $3.1 billion for a 10% stake. RBS will also get a seat on BoC's board.

The giant stumbles

Wal-Mart posted its smallest percentage increase in quarterly profits for four years. Net income rose to $2.8 billion in the second quarter, 5.8% higher than a year ago. The world's largest retailer also lowered its earnings forecast for 2005, partly because it thinks higher petrol prices will dampen spending by its core low-income customers.

Talks continued between **Northwest Airlines** and unions in an attempt to head off a strike by mechanics. America's fourth-biggest carrier is seeking to cut $1.1 billion in labour-related costs to avoid bankruptcy. Meanwhile, **British Airways** resumed flights after a strike provoked by the sudden dismissal of workers at a separate firm that provides the airline's catering. The industrial action could cost BA over £40m ($72m).

Agilent Technologies, a firm based in Palo Alto that specialises in scientific-testing equipment, sold its semiconductor business for $2.7 billion to **Kohlberg Kravis Roberts** and **Silver Lake Partners**. The two private-equity firms claim that the deal will create the largest privately held, independent chipmaker in the world.

Gateway, a personal-computer manufacturer based in southern California, reported its first quarterly profit since 2001, largely owing to a recent settlement with Microsoft. However, the company said an aggressive pricing strategy by Hewlett-Packard will affect future revenue. Last week, **Dell** also cut its sales forecast because of price competition, causing its share price to fall.

Still counting the costs

J. P. Morgan Chase and **Toronto-Dominion Bank** agreed to settle their part in a lawsuit brought by **Enron** against ten banks that it alleges "aided and abetted" the accounting fraud which led to the energy trader's bankruptcy in 2001. J. P. Morgan will pay $350m and Toronto-Dominion at least $70m. Enron is using the cash to pay its creditors.

American authorities accused BP, the British oil giant, of "systematic lapses" in safety and called for an independent review of safety at its five refineries. In March an accident at BP's Texas refinery killed 15 people and injured 170.

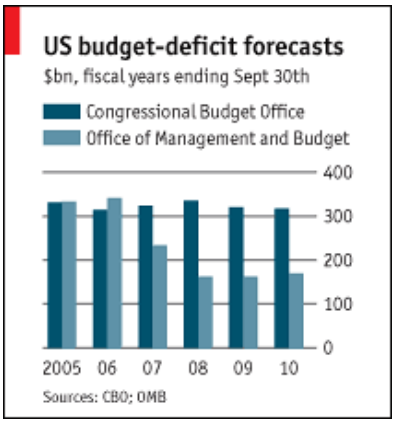
Reliant became the last independent energy-producer to settle with California and local utilities for allegedly manipulating prices in 2000-01, during the state's power crisis, and will pay $445m. Based in Texas, the firm controlled 8% of California's electricity.

After punching through $67 a barrel for the first time late last week, **oil prices** fell back to $63. Both Britain and the United States reported upticks in their **consumer-price inflation** rates this week, blaming rising energy costs.

The truth is out there

The non-partisan Congressional Budget Office estimated that America's **budget deficit** for the current fiscal year will be $331 billion, an improvement on last year and broadly in line with the White House's (OMB) estimate published last month. But the CBO forecast higher deficits for the near future, since it does not think recent increases in federal revenues are sustainable and assumes more cash will be required to keep troops in Iraq.

See article



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Letters

Aug 18th 2005
From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG
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Effective humanitarian aid

SIR – You rightly note the urgency of a meaningful response to the continuing attacks on Darfur's population by the government of Sudan and its proxy *janjaweed* militia ("Death and division", August 6th). But while a "bridging-force" of NATO troops to assist African Union peacekeepers would no doubt be helpful, such a response would take some time to assemble, even if there were a summoning of the will to put boots on the ground. Time is certainly not on the side of the refugees and displaced of Darfur. A far more rapid NATO response that would encounter less resistance would be to establish a no-fly zone over the region from French bases in neighbouring Chad. Retired General Merrill McPeak, former chief of staff of the United States Air Force, has estimated that a squadron of 12-18 fighters and four AWACS aircraft would successfully deter or neutralise Sudanese airpower. This would represent a useful interim response, as Sudanese helicopters and fixed-wing aircraft have been instrumental in attacks on villages. It would also be well within the means of NATO or a combined task-force composed of NATO members. This help should be offered to the African Union mission immediately.

Eric Witte
Beggen, Luxembourg

Reforming the Arab world

SIR – Charlemagne's focus on transatlantic co-operation in democratic reform of the Arab world is welcome and timely, especially the distinction he sees between the EU's cautious approach and Washington's "freedom agenda" (July 23rd). But Europe's caution is worse than he thinks. The EU's Neighbourhood Policy, which includes Arab countries among its partners, does not even contain the word "democracy". And the Democracy Initiative, run by the EU Commission and the only EU aid programme able to act without a host country's consent, spends only 4% of its €137m budget in the Middle East (the Commission now plans to abolish the Initiative).

At a conference in Venice last month, 120 Arab reformers called on the international community for an "independent and specific funding mechanism for civil-society activities to support democracy and reform". Washington not only promotes democracy through mainstream programmes, but also funds the excellent National Endowment for Democracy, which is a flexible and effective agency. Brussels needs similar mechanisms. After all, this is Europe's neighbourhood.

Edward McMillan-Scott MEP
Vice-President,
European Parliament
Brussels

Price promise

SIR – While the commitment of Whole Foods Market to organic foods is laudable, the same cannot be said of its exorbitant pricing policy (Face value, July 30th). Quite simply, its prices are outrageous—many people in America call Whole Foods "Whole Paycheque". It may be permissible to charge those prices now, but as Wal-Mart enters the market for organics, Whole Foods runs the risk of being seriously undercut.

Bill Jones

Pasadena, California

Teacher assessment

SIR – You claim that bad teachers in California "who scrape through their first couple of years are more or less assured of tenure for life" ("A hard slog", August 6th). Tenure for school teachers does not exist in California. They are granted a "permanent" job after two years of probation, but this permanent status merely gives them a right to a hearing before being sacked, which can happen under existing law on any number of grounds. Arnold Schwarzenegger's half-baked plan to extend teachers' probation to five years is not backed by research showing that it will improve teaching or learning in any way. But that is not what it is meant to do. Rather, it is a public-relations tool that simply maintains his crusade of teacher-union bashing.

In the real world, away from the movies, there are consequences that stem from bad policies. At a time of poor conditions in our underfunded public-school system, attacking teachers will convince many bright young people to choose another career.

Fred Glass
California Federation of Teachers
Oakland, California

The Chinese takeover

SIR – Your interpretation of CNOOC's failed bid for Unocal as "China bashing" fails to recognise the central issue of the entire affair: reciprocity ("Giving China a bloody nose", August 6th). In countries like the United States and Britain, there are well-defined paths that the prospective buyer of a company can follow to have a case heard and voted on by the target company's board and shareholders. These rules have provided for the takeover of hundreds of American and British companies by foreign corporations over the decades. Yet there is nothing even remotely resembling these rules to allow for the purchase of Chinese assets by foreign companies. To do business in China, let alone buy Chinese assets, even the mighty Wal-Mart must partner with a Chinese firm to help it navigate a ghastly maze of local red-tape and corruption that has precluded the participation of many foreign firms.

Eric Brosio
Petaluma, California

SIR – When the day comes that the communist Chinese government countenances allowing, for example, Exxon Mobil to buy CNOOC without whipping up a xenophobic frenzy, then I will rethink my opposition to supporting the business and geopolitical interests of that brutal dictatorship. Not everything in the world can be reduced to an argument about trade.

Bernard Mulligan
Providence, Rhode Island

Nuclear nations

SIR – You refer to India's hope of becoming a "fully legitimate nuclear power, alongside the existing five" ("Now we are six", July 23rd). This is a misunderstanding as there are no "fully legitimate" nuclear powers. The Nuclear Non-Proliferation Treaty of 1968 did no more than acknowledge that, at that date, some states had nuclear weapons and some did not. Those that did were charged (Article VI) with the obligation of negotiating their elimination. This obligation was expressed in even stronger terms in 1996 by the International Court of Justice. Since, even now, there are no negotiations in progress or contemplated anywhere aimed at the elimination of all nuclear weapons, no nuclear- weapon state has any claim to legitimacy in this area.

Bruce Kent
Campaign for Nuclear Disarmament
London

A tip about taxis

SIR – London cabs may work well in low speed, urban Manhattan ("A joy to hail", August 6th). However, I've had the displeasure of being taken in a London cab at high speed to the airport and was shaken to the bone in a kidney-rattling journey (and I've ridden in military vehicles). A joy to hail? More like a

joyless hell.

Roger Wilson
Falls Church, Virginia

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European economies

Germany's surprising economy

Aug 18th 2005
From The Economist print edition

The reviving health of a previously sick country

AT FIRST blush the news from Germany seems wearisomely familiar. In the second quarter, Europe's biggest economy tipped back to zero growth once more. Although unemployment is at long last starting to fall, the number out of work is still almost 5m, a shocking 11.6% of the workforce. Consumer spending seems stifled by lack of confidence in the future. And the centre-left government's plans for more reforms to the labour market, the welfare state, health care and the tax system were all put on hold in May, when Chancellor Gerhard Schröder called an early election for September—which, in another case of déjà vu, he is trying to win, as he did in 2002, with the help of an attack on American hints of military intervention in the Middle East, this time in Iran rather than Iraq.

It all sounds depressingly like a rerun of the same old story. But behind it lurks another, altogether more hopeful one. Thanks to the intense pressure that they have been under in the past few years, Germany's big companies have restructured and cut their bloated cost base. This process has for once been helped by the trade unions, which had been a stubborn obstacle to change. German workers have belatedly recognised that change has become essential, which is why they have been ready over the past year or so to accept such innovations as more decentralised pay bargaining, longer hours and even wage cuts. Thanks in part to this new flexibility, unit labour costs, a benchmark of competitiveness, have fallen sharply relative to other countries. In the past five years, Germany, long the most costly place in Europe in which to do business, has won a new competitive edge over France, Italy, the Netherlands and even Britain. That is a big reason why, last year, it regained its position as the world's biggest exporter.

Given this corporate turnaround and strong export performance, it is not surprising that both profits and the stockmarket have been rising sharply. More significantly, recent surveys of business confidence have been encouraging. Consumers remain nervous, largely because they are still fretful about their jobs; but, with unemployment now starting to come down, consumer confidence looks set to revive too. This suggests that domestic demand, the weakest link in the German economy, may be poised for a rebound. Indeed, some forecasters are now predicting that Germany, which has for so many years disappointed on the downside, could be about to surprise on the upside (see article).

Spreading its wings

The impact of such a turnaround would be felt far beyond Germany's borders. What happens in

Germany is critical for the rest of Europe, and thus for the world economy too. There are many reasons why the continent's economic performance has been so lacklustre since the heady days almost six years ago, when it launched its single currency, the euro. But the near-stagnation of Germany, which accounts for nearly one-third of euro-area GDP, lies at the root of most of them. So long as its biggest economy is stuck in a rut, the euro area as a whole is bound to remain stuck too. Germany's ills have also cast a shadow over other neighbouring economies dependent on its market, such as those of central Europe.

That is also why the German election, scheduled for September 18th, matters, and not just in Germany. As it happens, despite Mr Schröder's recent invocation of Iran, there is little chance of its being a rerun of September 2002, when he came from behind to snatch a narrow victory. It is true that the election no longer looks a shoo-in for the centre-right under Angela Merkel, partly because she has shown herself unusually gaffe-prone, and partly because of the rise of a new Left Party in Germany (see article). But the outcome is almost certainly not going to be another win for Mr Schröder's party: it will be either a clear victory for Ms Merkel, or a messy result in which her party emerges as the biggest, but is forced into a “grand coalition” with the centre-left.

On one level, the restructuring of corporate Germany and the glimmerings of a revival of business and consumer confidence should augur well for the economy whatever the election result. But on another, the commitment of the new government to further reforms will make a big difference. The politicians may not be able to control the economy, but they can certainly muck it up. A centre-right government under Ms Merkel would have the advantage that her party also controls the upper-house Bundesrat, making it far easier to push through legislative change. Conversely, if a grand coalition is assembled by politicians who see the election as confirmation of voters' resistance to change, the entire reform process could be shelved. That could quickly knock business confidence back, reverse the positive trend in unemployment and nip an incipient revival of consumer spending in the bud.

The new government needs to be careful about taxation as well. It is true that the outlook for Germany's public finances is dreadful, but any talk of higher taxes to fix the problem is decidedly premature. Corporate and income taxes need to be cut, not raised. The opposition's call for a two-point increase in value-added tax is dangerously reminiscent of the consumption tax imposed by the Japanese government in 1997, which set back an incipient recovery in the economy for several years (and thereby, incidentally, failed to improve the public finances). Tax increases are not what the German economy needs right now. A better idea would be to cut government subsidies, and to defer any indirect tax rises into the future, thereby both reassuring markets that a messy fiscal situation will be dealt with eventually and encouraging consumers to accelerate long-deferred spending plans.

The sickly German economy has been infecting the neighbourhood ever since the brief euphoria that followed unification in 1990 withered away within a few years. Indeed, Europe and the rest of the world have become so used to Germany's economic malaise that they have largely missed the recent signs of its revival, both in business and in the wider economy. The story from Germany is about to become surprisingly good—so long as the politicians do not foul it up after next month's election.

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Sri Lanka

The target was peace

Aug 18th 2005
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The assassination of the foreign minister raises the spectre of renewed war

AP

Get article background

IT IS a mark of just how poisonous the political situation in Sri Lanka has become that the assassination of the country's foreign minister on August 12th is being blamed on both sides: on the Tamil Tigers and on Sinhalese nationalists, perhaps linked to the security services, who oppose any deals with them. But whatever the truth about the death of Lakshman Kadirgamar—and the Tigers looked by far the likelier culprits this week—there is again a terrible risk that the country will slide back into full-blown civil war.

That would be a tragedy anywhere, but all the more so in Sri Lanka's case because three years ago there was genuine hope of a settlement, and also because the country suffered so appallingly in the tsunami of December 26th last year. Along with the Indonesian province of Aceh, also wracked by separatist conflict, Sri Lanka took the brunt of the devastation. It lost 30,000 of the 300,000 lives that were taken, more than any country outside Indonesia.

The tsunami's one redeeming feature was that all over the world it encouraged people to reach out across lines of conflict to succour and rebuild. Australia's hugely generous offer of $760m to Indonesia, for example, helped to repair tense relations, and in Indonesia's province of Aceh the relief effort helped create a fresh dynamic for peace. Negotiations there restarted, and this week a peace agreement was signed in a civil war that has spluttered on and off for 29 years (see article). Indonesia's president, Susilo Bambang Yudhoyono, said that a similar mechanism might now be applied to end his country's other long-running conflict, in Papua.

In Sri Lanka, which has likewise known almost constant, deadly conflict for more than 20 years, the same effect was hoped for. But the billions of dollars of assistance on offer have served only to stoke more arguments. The biggest has been over the establishment of a joint mechanism for distributing aid in the north and east of the island that the Tigers claim as a Tamil homeland or “Eelam”. The government and its aid donors hope that the flow of aid might lead to the resumption of peace talks, which broke down in 2003. But the government's agreement with the Tigers on how to distribute the aid has been strongly opposed by many Sinhalese, who see it as a first step towards the disintegration of their state.

Even before Mr Kadirgamar's assassination, the ceasefire established in 2002 was in danger of breaking down (see article). The Norwegian-led international monitors have reported a steady rise in the number of violations, with the Tigers invariably the worst offenders. It has hardly helped that the Tigers

themselves have faced an internal rebellion, opportunistically backed by sections of the Sri Lankan army. Nor have the Tigers ever really dropped their aim of total independence, despite sometimes hinting that they might be prepared to settle for substantial autonomy within a federal Sri Lanka.

Autonomy was already a brave thing for the government of President Chandrika Kumaratunga to offer, and there is no realistic chance that independence could ever be accepted by the majority Sinhalese. And nor should it be, if that would mean handing over a new statelet to the Tigers, whose claim to be the sole voice speaking for Tamils is based mainly on terror. The solution in Aceh has required compromise on both sides; in Sri Lanka, only the government has offered any of it. It is time for the Tigers to do the same, but at the moment all they are offering is more murder.

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Famine relief

Starving for the cameras

Aug 18th 2005
From The Economist print edition

People dying from hunger like those in Niger should not have to wait for the TV crews to arrive

EPA

THE Famine Early Warning Systems Network, known as FEWS Net, monitors the threat of mass hunger in some of the poorest parts of the world. It is hardly surprising, then, that FEWS Net has published an inquiry into the world's failure to respond to food shortages in Niger and the rest of the Sahel. The report is subtitled simply: “What went wrong?” That is the right question to ask. But what is surprising, and disconcerting, is that the report was written in 1997, not 2005.

This illustrates two things: Niger's present nightmare is a recurring one; and whatever went wrong in 1997 was not put right by 2005. In both cases, signs of distress were recognised early, but the response was dilatory. In both cases, relief agencies and donors failed to settle on an assessment of need. The decisive difference is that, in 1997, the international media were largely absent. In 2005, by contrast, the drought of attention eventually turned into a deluge. The Niger appeal received more money in the ten days after the media arrived on the scene than it had in the previous ten months. As a result, the worst may now be over there (see article).

Unfortunately, the media will always arrive late, if at all. Famine is a complex process, not a single, abrupt event (see article). Food prices rise, families sell their assets, some migrate in search of work or wild foods. As hunger sets in, the body's own assets decline. It is only after stomach muscles have wasted that the distended bellies so sadly familiar from television pictures appear. These images have become necessary to the genre. The falling livestock prices that long preceded them are not as telegenic.

Hunger also prevails far beyond the media spotlight. According to FEWS Net, many more people are affected by continuing food crises in Ethiopia, Somalia, Zimbabwe and Sudan. In each of those countries, there are also many hungry and dying babies. But the bright light the media sheds on its chosen subject throws everything else into shadow.

The bandwagon dilemma

The media attention now devoted to Niger and the political weight it carries pose a tactical dilemma for the aid agencies. Do they slow the bandwagon down to try to redirect it to other destinations it might otherwise bypass? Or do they take advantage of the media spotlight to wring as much money out of

donor governments as they can?

To downplay the crisis carries a big risk: there is a high political price to pay if one is seen as not doing enough in the face of such hardship. But there are equal and opposite dangers. Inevitably, the media sometimes overstate things. Loose talk of famine and millions of starvation deaths can do more harm than good. Such talk can tempt private traders to hoard grain, either out of fear that they, too, will succumb to famine or out of greed, anticipating the higher prices an international relief effort will pay. Media reports may also have prompted Niger's neighbours, from which it normally buys food, to restrict exports of grain to the country.

Famine is preventable because it is predictable. The job of foreseeing it falls to the early warning systems, such as FEWS Net, which is funded by the American government, and its UN counterpart. The job of preventing it falls first and foremost to the World Food Programme, another UN agency, plus a long train of private agencies. The job of funding their efforts falls to no one in particular. But then, when the cameras arrive, it falls to everyone at once.

Last year, Hilary Benn, Britain's minister for international development, made two proposals that now look more timely than ever. The most obvious one is to establish a standing fund on which relief agencies can draw. Such a fund should not free these agencies from accountability to their donors. But it should spare them from the need to court their paymasters in a panicked response to every emergency.

Early interventions are not only cheaper than belated ones. They can also avoid some of the dangers of food aid. Cheap food dumped on local markets for long periods might save some from starvation, but it can also hurt farmers, perversely eroding a country's agricultural capacity in the name of food security. In Ethiopia, which in 2003 received food aid equivalent to 15% of its annual cereal production, agricultural yields have stagnated. An early intervention that arrives before people's livelihoods are destroyed and before they are too weak to work can offer cash or vouchers with which to buy food on the market, rather than emergency rations to keep them alive.

Mr Benn's second proposal is that one agency, such as the European Commission's humanitarian agency ECHO, be designated a “financier of last resort”, a kind of swing provider of aid, whose job is to cater to the crises every other donor neglects. Both proposals have merit. The world's system for fighting the direst cases of mass hunger should not rest on a global sympathy contest umpired by television cameras.

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Health-care finance

Beware the doctors' diagnosis

Aug 18th 2005
From The Economist print edition

It's the way you spend the money that matters, not the way you raise it

Get article background

ACROSS the developed world, health-care spending is rising and will continue to increase as populations age. As each country feels the financial strain, it is tempting to imagine that there must be a better way of funding medical care elsewhere. In Britain, for example, Bernard Ribeiro, the new president of the Royal College of Surgeons, has called for the National Health Service (NHS) to be financed from social-insurance contributions, as in Germany and France, rather than from general taxation. He worries that a tax-financed system will not deliver enough resources to meet the demand for health-care spending in the longer run.

There are indeed good reasons for concern about the way the NHS is financed, for it has allowed the government to pump in too much money too fast. But there is no ideal system for paying for health care. The European social-insurance model is in even more trouble than Britain's tax-based model. By loading the burden on to employers and workers and thus raising labour costs, it has contributed to the inflexibility of labour markets and thus to the Euro-sclerosis that continental governments are struggling to recover from. In France, the government has resorted to general taxation to spread the burden. In Germany and elsewhere the model looks increasingly unsustainable, not least because its narrow fiscal base will be exposed to unfavourable demographics when the post-war baby-boomers start leaving the labour force in droves.

Nor does America offer an ideal solution. It has a mixed financing system, in which the government stumps up for the elderly and the poor, and employers pay for private coverage of their workers. Health-care spending has reached a record 15% of GDP, dwarfing Britain's 8%, yet 45m Americans lack insurance cover. The rising cost of publicly-financed medical care threatens America's fiscal health.

Rather than focusing on how the money is raised, reformers should worry about how it is spent. Health-care expenditure is rocketing not just because demand is rising but also because health-care markets work badly. They are dominated by powerful providers—companies, hospitals and influential doctors—which find it fairly easy to pass on ever-rising costs from new medical technologies to the state or the insurers who pick up most of the tab. Private individuals' payments generally account for a smallish share of health-care spending precisely because medical bills tend to be so high that everybody needs insurance cover of one sort or another. Taxes, social-insurance contributions and payments by employers all boil down to forms of health insurance.

The cure is not to try to raise yet more money in a different way. Instead, the overriding goal must be to spend the money pouring into health care more effectively by getting wasteful medical systems to work better. Two sets of reform are vital and both, as it happens, are being undertaken in Britain's tax-financed NHS.

The British model

The first set of reforms introduces more competition into health markets. The government has already broken the link between state funding and state provision by embarking on a big drive to buy non-emergency treatments from private-sector providers for publicly-funded patients. After the May general election, the government said it would push independent provision further. Within the health service, more and more NHS hospitals are being granted “foundation” status, which gives them more independence and thus encourages them to compete for business.

The second set of reforms is making the NHS a more efficient buyer of health care. The government is trying to do this by getting an internal market working within the NHS. Its most powerful weapon is a new payments system under which hospitals are paid according to the amount of work they do.

Naturally the pattern of reforms varies from one country to another. But in developed economies, there is now a drive to tackle the roots of rising health-care costs by getting medical markets to function more effectively. Such reforms are uncomfortable for doctors. They are meant to be. They are designed to wring better performance out of the medical profession and the health service.

It is the job of governments to try to get more health care for the money that people pay. It is the job of doctors' leaders to get more money for the health care they provide, and to avoid the unpleasant business of having to change their ways. They must be resisted.

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Terrorism

Lessons from anarchy

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Today's jihadists, like yesterday's anarchists, will fade. Terrorism won't

Mary Evans

ON THE face of it, anarchists, who believe in no government, have little in common with jihadists, who believe in imposing a particularly rigid form of government on everyone. The theoreticians for both movements have often been bearded and angry, of course, and their followers have readily taken to the bomb. But there the similarities end, don't they, so what lessons can be drawn from a bunch of zealots who flourished over 100 years ago and whose ideology now counts for practically nothing?

At least two, actually. The first is that repression, expulsion and restrictions on free speech do little to end terrorism. All were tried, often with great vigour, at the end of the 19th century when the anarchist violence that terrified much of Europe and parts of America was at its zenith. As our report makes clear, governments had good reason to respond. Austria, France, Italy, Spain and the United States all lost an empress, king, president or prime minister to anarchist assassins. Such murders were so common that King Umberto of Italy, throwing himself aside to escape a stabbing, casually remarked, “These are the risks of the job.” (He was later shot dead.) Anarchists also killed lots of less exalted innocents.

Then, as now, governments responded to the clamour for action with measures to criminalise anyone preaching or condoning violence and, if they were foreign, to keep them out of the country. Spain brought in courts-martial for bombers, foreshadowing perhaps America's military commissions for Guantánamo trials. Britain, with a tradition of tolerating dissent, became home to many continental radicals, such as those driven out of Germany after the two attempts on Kaiser Wilhelm I's life in 1878. Britain, however, was not afflicted with bombings as other countries were. Spain, where every kind of retribution including the crudest of tortures were the standard response, suffered many more outrages. Yet few lessons seem to have been learnt. Several of the new measures announced on August 5th by Tony Blair, Britain's prime minister, echo almost exactly those passed in France after a bomb had been lobbed into the French parliament in 1893.

In both Britain and America, new attacks are said to be inevitable. Yet every new attack is followed by new measures, as though such measures could have averted an inevitability had they been in place before. They could not, both logically and because terrorism cannot be defeated, as countries can be. That is the second lesson to be drawn from the anarchists.

The enduring allure of idealism and violence

Throughout history, men seized with a sense of injustice, or purpose, or hatred, or inadequacy, have resorted to bloodshed. The anarchists were not the first. They were merely particularly potent believers in violence in the furtherance of an idealistic, millenarian vision. Jihadists are too. Most anarchists, like most Islamists, were not violent. But, like the jihadists, they had their firebrands and, like the jihadists, they had an ideology that could be twisted to appeal to a certain kind of wounded utopian lacking all capacity for empathy.

Such people can be caught, sometimes before they have done anything terrible. That argues for excellent intelligence and police work. Perhaps their numbers can be reduced by ameliorating the grievances that lend them the justification for their attacks. That argues for political action. And certainly the public needs reassurance. That argues for honest explanation—that terrorism does not threaten any western government, that retribution, like police injustices committed in nervous haste, is likely to provoke more violence, that new restrictions are unlikely to bring new safety. Honest explanation, and simple history, also suggest that this wave of terror will pass, just as the anarchist wave passed, but that terrorism will not—not as long as strange men are captivated by strange ideas. The jihadists will go. Others will take the stage.

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The anarchists

For jihadist, read anarchist

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From The Economist print edition

Mary Evans

Repression did little to stop anarchist violence. But eventually the world moved on and the movement withered

BOMBS, beards and backpacks: these are the distinguishing marks, at least in the popular imagination, of the terror-mongers who either incite or carry out the explosions that periodically rock the cities of the western world. A century or so ago it was not so different: bombs, beards and fizzing fuses. The worries generated by the two waves of terror, the responses to them and some of their other characteristics are also similar. The spasm of anarchist violence that was at its most convulsive in the 1880s and 1890s was felt, if indirectly, in every continent. It claimed hundreds of lives, including those of several heads of government, aroused widespread fear and prompted quantities of new laws and restrictions. But it passed. Jihadism is certainly not a lineal descendant of anarchism: far from it. Even so, the parallels between the anarchist bombings of the 19th century and the Islamist ones of today may be instructive.

Islamists, or at least those of the Osama bin Laden stripe, have several aims. Some—such as the desire "to regain Palestine", to avenge the killing of "our nation's sons" and to expel all "infidel armies" from "the land of Muhammad"—could be those of any conventional national-liberation movement. Others are more millenarian: to bring everyone to Islam, which, says Mr bin Laden, "is the religion of showing kindness to others, establishing justice between them, granting them their rights, and defending the oppressed and persecuted." All this will come to pass once everyone is living in an Islamic state, a caliphate governed by *sharia* law. Hence "the martyrdom operations against the enemy" and the promise of paradise for those who carry them out.

Anarchists have always believed in the antithesis of a Muslim state. They want a world without rule. Their first great theoretician, Pierre-Joseph Proudhon, wanted to abolish centralised government altogether. This, though, would not bring the chaos with which the word anarchy is often considered synonymous. On the contrary, a sort of harmonious order would ensue, the state being replaced by a system of autonomous groups and communities, glued together by contract and mutual interest in place of laws. Justice, argued this essentially non-violent man, was the "central star" governing society.

Though Proudhon is remembered for the dictum, "Property is theft!" he actually believed that a man had the right to possess a house, some land and the tools to work it. This was too much for Mikhail Bakunin, a revolutionary nationalist turned anarchist who believed in collective ownership of the means of production. He believed, too, that "the passion for destruction is also a creative urge," which was not a description of the regenerative workings of capitalism but a call to the barricades. Regeneration, however, was very much an anarchist theme, just as it is a jihadist one. As one of anarchism's leading

interpreters, George Woodcock, has put it, “It is through the wrecks of empires and faiths that the anarchists have always seen the glittering towers of their free world arising.”

What prompts the leap from idealistic thought to violent action is largely a matter for conjecture. Every religion and almost every philosophy has drawn adherents ready to shed blood, their own included, and in the face of tyranny, poverty and exploitation, a willingness to resort to force is not hard to understand. Both anarchism and jihadism, though, have incorporated bloodshed into their ideologies, or at least some of their zealots have. And both have been ready to justify the killing not just of soldiers, policemen and other agents of the state, but also of civilians.

The heads roll

For anarchists, the crucial theory was that developed in Italy, where in 1876 Errico Malatesta put it thus: “The insurrectionary deed, destined to affirm socialist principles by acts, is the most efficacious means of propaganda.” This theory of “propaganda by deed” was cheerfully promoted by another great anarchist thinker, Peter Kropotkin, a Russian prince who became the toast of radical-chic circles in Europe and America. Whether the theory truly tipped non-violent musers into killers, or whether it merely gave a pretext to psychopaths, simpletons and romantics to commit murders, is unclear. The murders, however, are not in doubt. In deadly sequence, anarchists claimed the lives of President Sadi Carnot of France (1894), Antonio Cánovas del Castillo, the prime minister of Spain (1897), Empress Elizabeth of Austria (1898), King Umberto of Italy (1900), President William McKinley of the United States (1901) and José Canalejas y Méndez, another Spanish prime minister (1912).

Such assassinations, it may be argued, were less similar to al-Qaeda's than to those of the Narodniki, the members of the Russian Party of the People's Will, who believed in “destroying the most powerful person in government” to undermine its prestige and arouse the revolutionary spirit. This they had undoubtedly done in 1881 by murdering Tsar Alexander II, even though he had been a reformer and, indeed, a liberator of the serfs. In truth, the practice of assassination is as old as the hills, though it got its name only in the 11th-13th centuries when it was followed by the Nizari Ismailiyun, a Shia sect that considered the murder of its enemies—conducted under the influence of hashish (hence assassin)—to be a religious duty.

Mr bin Laden would surely delight in some dramatic assassinations today. Presidents and prime ministers, however, do not nowadays sit reading the newspaper on the terraces of hotels where out-of-work Italian printers wander round with revolvers in their pockets, as Cánovas did, or walk the streets of Madrid unprotected while looking into bookshop windows, as Canalejas did. So Mr bin Laden must content himself with the assertion that on September 11th, “God Almighty hit the United States at its most vulnerable spot. He destroyed its greatest buildings...It was filled with terror from its north to its south and from its east to its west.”

The anarchists, too, were happy to resort to more indiscriminate acts of terror. “A pound of dynamite is worth a bushel of bullets,” said August Spies, the editor of an anarchist newspaper in Chicago, in 1886. His readers evidently agreed. A bomb thrown soon afterwards was to kill seven policemen breaking up a strikers' gathering in the city's Haymarket Square.

France, too, had its *dynamitards*. One of their bombs blew up the Restaurant Véry in Paris in 1892. Another, some months later, which was destined for a mining company's offices, killed six policemen and set off a flurry of wild rumours: acid had been placed in the city's water supply, it was said, churches had been mined and anarchists lurked round every corner. A year later a young anarchist, unable to earn enough to feed himself, his lover and his daughter, decided to take his own life—and at the same time make a protest. Ready to bomb but unwilling to kill, he packed some nails and a small charge of explosive into a saucepan and lobbed it from the public gallery into the Chamber of Deputies. Though it caused no deaths, he was executed—and then avenged with another bomb, this one in the Terminus café at the Gare St-Lazare which killed one customer and injured 19. The perpetrator of this outrage, designed to “waken the masses”, regretted only that it had not claimed more victims. A popular street song boasted:

> It will come, it will come,
> Every bourgeois will have his bomb.

And many were inclined to agree. Four more bombs went off in Paris in the next two months.

Other countries were hardly more peaceful. A bomb was lobbed into a monarchist parade in Florence in 1878, another into a crowd in Pisa two days later. In 1893, two bombs were thrown into the Teatro

Liceo in Barcelona, killing 22 opera-goers on the first night of the season. A year later a French anarchist blew himself up by accident in Greenwich Park in London, presumably on his way to the observatory there. Two years later, at least six people taking part in a religious procession in Barcelona were blown to bits by an anarchist bomb. Countless attempts were also made on the lives of bigger names, such as King Alfonso XII of Spain (1878), Kaiser Wilhelm I of Germany (May and June 1878), Andrew Carnegie's business partner, Henry Clay Frick (Pittsburgh, 1892), a Serbian minister (Paris, 1893) and King Alfonso XIII and his English bride (Madrid, on their wedding day, 1906). In this last incident alone 20 bystanders died.

Then, as now, alarm and consternation broke out. Admittedly, violent attacks on prominent figures were quite frequent: one American president had been assassinated in 1865 (Lincoln) and another in 1881 (Garfield), and seven attempts were made on Queen Victoria's life before her reign ended in 1901, none of them by anarchists. Even so, governments could hardly do nothing. The response of some was repression and retribution, which often provoked further terrorist violence. Germany arrested 500 people after the second attack on the kaiser, many for “approving” of the attempts on his life. Spain was particularly prone to round up the usual suspects and torture them, though it also passed new laws. After the Liceo bombing, it brought in courts-martial for all crimes committed with explosives, and only military officers were allowed to be present during the trial of the supposed bombers.

France, too, resorted to unusual measures. After the bombing of the French Chamber of Deputies, 2,000 warrants were issued, anarchist clubs and cafés were raided, papers were closed down and August Vaillant, the bomber, was tried, found guilty and sentenced to death in a day. An apologist who declared that not a single man in France would grieve for the president if he confirmed the sentence (as he did), and then was assassinated (as he was), was jailed for two years for incitement to murder. The French parliament made it a crime not just to incite sedition but also to justify it. Criminal “associations of malefactors” were defined by intent rather than by action, and all acts of anarchist propaganda were banned.

Similarly, in Britain soon after last month's bombings, the prime minister, Tony Blair, announced that “condoning or glorifying terrorism” anywhere, not just in the United Kingdom, would become a crime. Places of worship used as centres for “fomenting extremism” are to be closed down. Measures will be taken to deport foreigners “fostering hatred, advocating violence to further a person's beliefs, or justifying or validating such violence.” Naturalised Britons engaged in “extremism” will be stripped of their citizenship.

Jihadists, of course, cross borders, and many are presumed to be indoctrinated by foreigners, even if they commit their deeds at home. So it was too with the anarchists, even though they often plotted and acted alone. Many of the ideas came from Russia. Besides Bakunin, Russia also produced Kropotkin, “an uncompromising apostle of the necessity of violence”, according to Barbara Tuchman in “The Proud Tower”.

Italy, by contrast, produced many of the assassins: for example, those who killed Carnot, Cánovas, Empress Elizabeth and King Umberto. It also exported utopians who founded anarchist settlements like the Cecilia colony in Brazil. Germany, too, had its share of fanatics, including Johann Most, the editor of an incendiary New York newspaper, *Freiheit*, and many of the Jewish anarchists who congregated in London's East End. France also sent *anarchos* abroad: a prominent theorist, Elisée Reclus, taught in Brussels. The man who shot McKinley was the child of Polish immigrants to America. And Switzerland, like England, played host to exiles who came and went with considerable freedom.

No wonder, then, that anti-foreigner feeling ran high in many places. In the United States, President Theodore Roosevelt asked Congress to exclude anyone who believed in “anarchistic principles” and, by treaty, to make the advocacy of killing an offence against international law. Congress duly obliged with an act that kept out anyone “teaching disbelief in or opposition to all organised government”.

By then an international conference had been held (in 1898) at the behest of Italy to seek help in fighting anarchism. The Italians did not get all they wanted: Belgium, Britain and Switzerland refused to abandon the right of asylum or to extradite suspected anarchists. But in 1893, just after the Liceo bombing, Britain had reluctantly banned open meetings of anarchists after the Liberal home secretary, H.H. Asquith, had come under attack for allowing an anarchist meeting to commemorate the Chicago Haymarket martyrs.

The vast majority of anarchists, like the vast majority of Islamists, were not violent, and some of those who once believed in bloodshed, notably Kropotkin, were to turn against it in time. But those who relished indiscriminate violence used an argument with striking similarities to that used by Mr bin Laden. Thus Emile Henry, who had left the bomb in the café at the Gare St-Lazare, was to justify his act by

saying that those in the café were all “satisfied with the established order, all the accomplices and employees of Property and the State...There are no innocent bourgeois.” For his part, Mr bin Laden, in his “Letter to America” of November 2002, justifies the “aggression against civilians for crimes they did not commit” with a slightly more sophisticated variant. They deserved to die, he said, because, as American citizens, they had chosen “their government by way of their own free will, a choice which stems from their agreement to its policies.”

Such sentiments recall the characters of Conrad's “The Secret Agent” and Fyodor Dostoevsky's “Devils”. Inspired by 19th-century anarchist intellectuals and events, they describe men of almost autistic lack of empathy and contorted moral sense. For Conrad's protagonist, nicknamed the Professor, the world's morality

> was artificial, corrupt and blasphemous. The way of even the most justifiable revolutions is prepared by personal impulses disguised into creeds. The Professor's indignation found in itself a final cause that absolved him from the sin of turning to destruction as the agent of his ambition. To destroy public faith in legality was the imperfect formula of his pedantic fanaticism; but the subconscious conviction that the framework of an established social order cannot be effectually shattered except by some form of collective or individual violence was precise and correct. He was a moral agent—that was settled in his mind. By exercising his agency with ruthless defiance he procured for himself the appearances of power and personal prestige. That was undeniable to his vengeful bitterness. It pacified its unrest; and in their own way the most ardent of revolutionaries are perhaps doing no more but seeking for peace in common with the rest of mankind—the peace of soothed vanity, of satisfied appetites, or perhaps of appeased conscience.

Anarchists like the Professor, a quiet man who went round with a bomb in his pocket that he could detonate with the squeeze of a rubber ball should he be arrested, were difficult to detect and impossible to deter. So why did their wave of terror pass? Not, it seems, because of the measures taken to deter them. The main reason, rather, was that the world became consumed with the first world war, the Russian revolution, the fight against fascism and the struggles against colonialism. Another was that, after a while, the more rational anarchists realised that terrorism seldom achieves the ends desired of it—as the IRA has recently acknowledged.

But in truth the wave did not entirely pass; it merely changed. The anarchist terrorists of 1880-1910 were replaced by other terrorists—Fenians, Serb nationalists (one killed the Archduke Franz Ferdinand and thus sparked the first world war), Bolsheviks, Dashnaks (revolutionary Armenians), Poles, Macedonians, Hindu nationalists (among them the killers of Mahatma Gandhi), fascists, Zionists, Maoists, Guevarists, Black Panthers, Red Brigades, Red Army Fractions, Palestinians and even al-Qaeda's jihadists. Few of these shared the anarchists' explicit aims; all borrowed at least some of their tactics and ideas.

And the world went on. It probably would even if yesterday's *dynamitards* become today's *plutoniumards*. But terrorism is unlikely to be expunged. As long as there are men like Conrad's Professor, there will be causes to excite them, and therefore deeds to terrify their fellow citizens.

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Financing health care

Searching for a miracle solution

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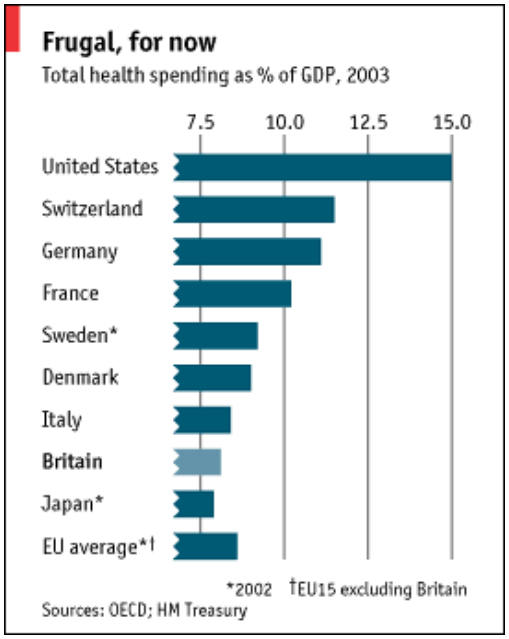
Rich countries everywhere are struggling to finance health care



Get article background

THANKS to the taxpayer, the National Health Service is currently enjoying an unprecedented boost to its finances. The NHS budget has doubled over the past eight years and the bonanza will continue until 2007-08. By then, total health spending will have risen from 6.8% of GDP in 1997 to 9.2%, higher than the latest average in the rest of the European Union.

So this might seem an odd moment for a senior doctor to call for a switch in the way that the NHS is financed. Yet that is what Bernard Ribeiro, the new president of the Royal College of Surgeons, has done. In an interview with the *Daily Telegraph* published on August 13th, he argued that a tax-based system will be unable to cope with future health-care demands. Instead, Britain ought to emulate the social-insurance model of Germany and France, in which the main source of finance is contributions levied on workers' pay.

Mr Ribeiro's intervention has re-opened a debate that Gordon Brown peremptorily closed in 2002. It was then that the chancellor of the exchequer announced a five-year cash settlement for the NHS stretching ahead until 2007-08. That appeared to resolve the issue, which did not feature in the general election.

What lies behind Mr Ribeiro's remarks is a concern about what will happen from the spring of 2008. That date, which once seemed so distant, is now looming. Doctors and health managers are starting to fret about the ability of the NHS to cope with more austere times.

But would a switch away from tax funding help? There are three main models of health-care finance in the developed world. In Britain, Canada and Sweden, among others, the principal source of revenue is general taxation. In many European countries, funding comes mainly from compulsory social-insurance contributions paid by workers and their employers. America is unusual in that private funding accounts for a much bigger share of total health-care spending because most workers and their families are

insured privately through their employers. Public spending, which goes mainly to the old and the poor, is financed through a mix of general taxes and payroll contributions.

The European and American models are becoming a bit more like the British one. In France, for example, social-insurance contributions are now buttressed by a general tax on income. In America, a big expansion of government spending on older people to help pay for their drugs bills will be financed from general tax revenues. And in Britain, Mr Brown pushed up social-insurance contributions in his 2002 budget to raise money for the surge in spending on the NHS.

This suggests it is unrealistic to expect any one model to deliver a more buoyant source of revenue. Across the developed world, health budgets are feeling the strain. In Germany and France, governments have had to push through reforms to try to constrain spending. In America, there is mounting concern about the spiralling cost of health care, which has risen to 15% of GDP.

Nor does any of the financing models clearly have an advantage in keeping a lid on health spending. Despite their apparent variety, they are all forms of insurance, which means that a third party picks up the tab, weakening the resistance to medical bills. These keep on rising because of expensive advances in medical technology in a marketplace where providers are particularly powerful since doctors determine what medical care is necessary.

In most insurance markets, competition between insurers puts pressure on the costs of providers. But competition between health insurers is ineffective because the commercial incentives are for insurers to compete for healthy patients, who cost little, and to exclude the sick, who cost a great deal. This is an argument for a single insurer, like the NHS, that can cover everyone and stand up to powerful medical providers. In practice, however, much of the extra spending on the health service in recent years under Labour has been absorbed in higher pay.

Finding an alternative source of finance is not the way forward for the NHS. Rather, the goal must be to get better value for the record sums of money being lavished on it. This is a lesson that the Labour government has learnt slowly and expensively. It began by throwing money at an unreformed NHS. Then it realised it had to drive a much harder bargain. Since 2002 it has been striving to intensify competitive pressures through two main reforms.

First, the health service is being reorganised as an internal market, in which money is not doled out to hospitals, but, rather, follows the patients and the treatments they need. A new payments system means that hospitals are paid according to how busy they are. That puts pressure on under-performing hospitals. High-performing hospitals that win “foundation” status are being encouraged to do even better since they can keep financial surpluses and reinvest them in services.

Second, hospitals are facing much greater pressure from outside the NHS. The government has turned to the private sector to provide more medical care, subverting the dogma that public funding must mean public provision. Since the general election, Patricia Hewitt, the health secretary, has announced a further wave of contracts to private providers. The aim is that by 2008 the independent sector will carry out around 10% of elective care, helping the government achieve its goal of a maximum waiting time of 18 weeks for non-emergency treatments.

A worry about the reform programme is that the purchasers in the internal market—the 300 or so local primary-care trusts that commission care for their populations—are not up to the job. So the government is seeking to pep them up. Many will merge and they will achieve greater focus on purchasing by shedding, where possible, their other function of providing some primary care themselves. Family doctors will be given a greater role, backed by budgetary incentives, in commissioning.

There is plenty to criticise in Labour's handling of the NHS. But the current direction of reform is the right one. Instead of yearning for new sources of extra revenue after years of bumper budgets, doctors should accept that securing better value for money must be the priority.

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History for children

Notes on a small island

Aug 18th 2005
From The Economist print edition

An old approach to history is new again

"ONCE upon a time there was a giant called Neptune." So begins "Our Island Story", a much-loved history of Britain for children by H.E. Marshall that was first published in 1905. The book has been out of print since 1953, when a special edition was published to mark the coronation of Elizabeth II. Next month Civitas, a think-tank that frets about the decline of social mores, is reissuing the book as a corrective to the trendy, disjointed history that is now taught in schools. Civitas also believes that, by giving Britons a story to be proud of, the book might even turn them into better citizens.

Britain lacks a good founding story. Other European countries had liberation movements that threw off foreign oppressors, or at least a decent revolution that swept away the old order. In Britain, many of the things that look like national symbols turn out to be Victorian fakes. The Houses of Parliament, for example, are coated in gothic details that seem to represent ancient liberties. But they were built long after the plans for Washington, DC, were drawn up.

"Our Island Story", with its stories about King Alfred's cakes and Maori cannibals in New Zealand, seems like an odd candidate to plug this gap. However, two current trends are on the book's side, and will ensure it a more sympathetic audience than, say, Helen Bannerman's "Little Black Sambo", another children's favourite in the early years of the 20th century.

First, senior politicians are musing on what being British is all about. Labour started doing this when it came into power in 1997. During its first term, the answers the party came up with involved ditching allusions to fusty traditions and insisting that Britain was a young country. Since 2001, when riots revealed how little whites and Asians mixed in some northern cities and September 11th showed how useful shared symbols like flags can be, this enquiry has become more urgent. It is also focused more on the past.

Gordon Brown, the chancellor, now routinely talks about venerable British values. Not surprisingly, he is particularly fond of the 18th-century Scottish enlightenment. David Blunkett, the pensions secretary, has eulogised England's landscape, sense of humour and radical traditions. John Denham, an influential former minister, thinks Britain needs a national story that includes an account of its global role in the 19th century, to explain why migrants from Commonwealth countries belong alongside Anglo-Saxons. A book that insists the English were not really defeated by the Normans fits the mood well.

The second thing that counts in the book's favour is that historians have rediscovered storytelling, and even fiction. Well-respected academics like Sir Norman Davies and Simon Schama have swapped the safety of narrow monographs for grand sweeps across the centuries. "Our Island Story" is still more cutting-edge. With its brave mix of truth and myth, it is impeccably postmodern.

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Public and private security

A thicker blue line

Aug 18th 2005
From The Economist print edition

Private security firms are suffering as the police get more powerful

EVER since four bombs exploded in London on July 7th, the police have put on a show of force. Armed officers loiter in front of public buildings, while brightly-clad police community support officers (PCSOs) patrol station concourses. The point is to deter terrorists, but there's another message, too. Even before the attacks, the police admitted that they wanted to dominate the security business. As Sir Ian Blair, commissioner of London's Metropolitan Police, put it: “We're trying to monopolise the market.”

The chief competition comes from some 130,000 people working for about 2,000 private security companies. They catch shoplifters, patrol housing estates and reassure the public—everything the police are expected, but have traditionally failed, to do, which is why private security companies proliferated in the first place.

Until recently, the police believed that private security companies were a necessary, perhaps even a welcome presence on Britain's streets. Sir Ian explained in a 1998 speech that the police ought to relinquish their monopoly over patrolling and become an overseer of security services. There was much talk of an “extended police family” consisting of coppers, guards and local-government workers. That metaphor is still used; but the police have taken on the role of stern father.

One reason the coppers are so cocky about their ability to dominate the market is that they have more uniformed bodies. There were 141,000 police officers at the last count, in March—up from 124,000 in 2000. They are joined by a new army of PCSOs, currently 6,200 strong but expected to number 24,000 by 2008. The PCSOs receive less training and fewer powers than sworn officers, which makes them cheaper. It also means they can stay on the streets and avoid becoming tied up with bureaucracy.

Unlike police officers, PCSOs can easily be sold to local authorities, housing associations and shopping malls, doing their bidding while remaining under the nominal control of the police. In London, buyers have been found for more than 600 officers, with most going to Transport for London, which manages the bus network. At a total cost of about £35,000 ($63,000) per year, they are more expensive than security guards, but a lot cheaper than sworn officers—and they have other advantages, such as police radios. Thanks to them, the police can compete against private providers. “PCSOs have skewed the market,” says Richard Childs, a former chief constable who is now a security consultant.

Another, unfair, aid to the police is that the competition is about to become a lot more expensive. Government regulations mean that, beginning next March, security guards will have to undergo four days' training and pass a criminal-record and background check. That will be expensive for employers and difficult for the immigrant workers on whom the industry relies. The result, according to the British Security Industry Association (BSIA), a trade body representing large and medium-sized operators, will be the immediate departure of around one in ten guards and a wage hike of 12-15%.

Smaller outfits are likely to disappear altogether, says Richard Evans, managing director of The Watch Security, which was acquired recently by a bigger fish. Regulation and a new “preferred contractor” scheme will reduce the number of suppliers—to 300, according to the BSIA; to perhaps 50, according to Bobby Logue, an industry analyst. That will alleviate competition in a notoriously cut-throat business, and perhaps even create some local monopolies. Further price increases will be the result.

Hazel Blears, a home office minister, does not want to see private security companies wiped out, although she is keen to see them kept in their place. The right to protection, she says, should not depend on the ability to pay. It's an admirable sentiment. The trouble is that, in future, there may be less protection to go round.

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Shooting to kill

Smoke signals

Aug 18th 2005
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Disturbing new revelations about a police killing

THE day after London's police shot dead Jean Charles de Menezes on a Tube train, they admitted it had been a case of mistaken identity. The building in which the Brazilian electrician lived was being watched because police believed that a man they suspected of trying to set off a bomb on July 21st was inside. When Mr Menezes emerged on the morning of July 22nd they thought he might be a terrorist, and decided to follow him. A combination of bad luck, police error and Mr Menezes's suspicious behaviour, police claimed, led to his death less than an hour later.

That Mr Menezes behaved suspiciously now seems dubious. Leaked documents from the independent inquiry into the shooting undermine the police's version of events. Rather than wearing an unnaturally warm coat on a summer's day, as the police implied, Mr Menezes was clad in a thin denim jacket. He did not jump the ticket barriers, but used his ticket and felt sufficiently relaxed to pick up a free newspaper. He walked calmly down the escalator, breaking into a run only in order to catch a train.

It also appears that Mr Menezes was not clearly identified by the surveillance team. The man who saw him leave the building was apparently urinating at the time, and was unable to switch on his video camera. Most worryingly, because of what it suggests about miscommunication between different branches of the police, one of the surveillance team told investigators that he had pinned Mr Menezes's arms to his sides before armed officers opened fire.

The most lurid and inaccurate media accounts of Mr Menezes's last moments, some of which suggested he had wires protruding from his body, were based on eyewitness accounts, not police statements. But the police failed to correct such stories, which bolstered their case that the killing was justified. Other sources let it be known that Mr Menezes's visa had expired—a revelation that was perhaps intended to explain why he might have behaved oddly.

It also emerged this week that Sir Ian Blair, London's police commissioner, contacted the Home Office soon after the shooting to ask whether the terrorism investigations might take precedence over an inquiry into the shooting. When that inquiry does report, later this year, its findings are likely to be troubling.

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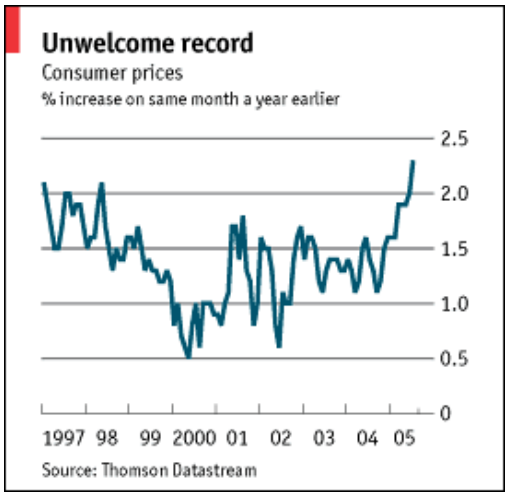
Interest rates

Unboring

Aug 18th 2005
From The Economist print edition

Monetary policy gets interesting



MERVYN KING, the governor of the Bank of England, has long aspired to make monetary policy boring. But the meeting, in early August, of the Bank's committee which sets interest rates was unusual.

For one thing, it was the 100th meeting since the Bank's Monetary Policy Committee (MPC) was given control over the level of interest rates by the incoming Labour government in 1997. For another, the MPC decided to cut interest rates from 4.75% to 4.5%. It was the first reduction in more than two years.

What's more, that decision was a close-run thing, as the minutes of the meeting, published on August 17th, revealed. Four of the nine-strong committee voted to keep rates on hold. More interesting still, Mr King was among the dissenters—the first time in the history of the MPC that the Bank's governor has been in a minority, although Mr King had been outvoted before as deputy governor.

The Bank had already signalled in its quarterly *Inflation Report*, released on August 10th, that rates were unlikely to fall much further, if at all. The divide on the MPC, together with Mr King's prominence as a dissenting voice, reinforces the view that the reduction in rates to 4.5% in early August might be the Bank's first and last cut in this phase of the interest-rate cycle.

A further reason to expect that rates will remain on hold is that the annual rate of consumer-price inflation has risen sharply, from 2.0% in June to 2.3% in July. Not only is that a record high in the short history of the series, which started in January 1997 (see chart). It is also uncomfortably higher than the government's 2% target. Only last September, inflation was as low as 1.1%.

In the Bank's *Inflation Report*, the upsurge in inflation is attributed partly to higher oil prices and partly to more general pressures arising from an economy operating close to capacity. The further acceleration in July appears to vindicate the fears of the four MPC members who voted against the rate cut. They worried that “adding to the strength of the recovery would risk adding to inflationary pressures while costs were still working their way through the supply chain”.

But will the economy stage a strong recovery after the recent period of weakness? That is the crucial question for the MPC. The answer, which lies in the hands of the consumer, will determine whether

interest rates will stay on hold or fall again. Whatever happens, Mr King is likely to be thwarted in his ambition to make monetary policy boring.

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Terminal 5

Blue skies thinking

Aug 18th 2005 | HEATHROW
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Heathrow's new terminal is on time and on budget. How odd

BIG construction projects are not a British speciality. The publicly-funded Millennium Dome was a well-publicised catastrophe that came in hundreds of millions of pounds over budget. Others, like the Channel Tunnel and the upgrade of the main train line from London to Glasgow, are less visible but equally troubled. Yet one big building project is going rather well. Four years after a lengthy public inquiry controversially approved a fifth terminal at Heathrow airport, it remains on time and on budget.

The project's scale is impressive. It covers 260 hectares, around the same as Hyde Park. Construction has meant shifting 6.5m cubic metres of earth and building a 13.5km tunnel network underneath working runways, as well as running one of the largest archaeological digs in the country. Some 67m passengers used Heathrow last year; Terminal 5 will have room for 30m more. The estimated price is £4.2 billion, financed through bonds. If history is any guide, a project this big should be doing disastrously. Yet Tony Douglas, the man in charge, is adamant: “Terminal 5 will open at 0400 on the 30th of March, 2008, as planned,” he says. Why the confidence?

New technology is one reason. Every wire, pillar and pipe is digitally modelled, which helps to prevent the costly mistakes that can arise if members of the design team are working under different assumptions about where bits of the building go. The entire project is contained in a single computer simulation, and individual parts of the terminal—such as the labyrinthine baggage-handling system—can be given a digital dry run. That's useful for preventing problems later on, since virtual mistakes are much easier to fix than real ones. Technology has helped in other areas, too. Just-in-time scheduling, borrowed from the manufacturing industry, means that very little needs to be stored on site.

But technology alone cannot explain the project's success, since plenty of other badly-run projects have benefited from similar technical wizardry. The most important difference between Terminal 5 and other large building projects has been the approach to project management, and especially to risk.

All large projects are risky, but BAA is particularly vulnerable to cost overruns. It can rely neither on the largesse of taxpayers nor on increased prices for its services (which are set by a regulator) to cover any unexpected costs. And the firm was involved in one of the worst civil engineering disasters of the past 30 years, when part of a tunnel for its Heathrow Express train service collapsed in 1994.

The firm studied many badly-run projects from the past, which led it to the conclusion that the traditional idea that risk could be passed on to suppliers by means of complicated contracts was a fiction. “If a supplier does a bad job, I might get a few million off him in compensation,” says Mr Douglas. “That's great, but it doesn't get my airport built.” And, he says, traditional contracts tend to lead to a misallocation of resources: “if you're a supplier, your best brains go into your legal department, so that when things go wrong you can write creative excuses.”

The Terminal 5 contract tries to align the interests of BAA and its suppliers so that risks can be managed properly. Risk payments, which are normally part of a supplier's quote, are instead put in a central pot. If a job is done on time, the firms get a cut. If there are problems, they are solved with money from the reserve. That also ensures that suppliers work together to sort out any snags, since problems caused by one firm cut the size of the bonus pot for the rest. Contractors share their books with BAA, which reduces the scope for waste (and creative accounting). The incentives seem to be working: BAA says that 80-85% of the jobs on site get finished on time, compared with around 60% for the rest of the building industry.

Some observers wonder if this approach might be useful elsewhere, especially in the public sector, where delays and cost overruns are particularly embarrassing. Stephen Glaister, of Imperial College, London, thinks that if Terminal 5 proves a success, the question of whether a similar model could be

applied to public contracts will be raised. A significant and growing chunk of government spending is done via public-private partnerships, which try to achieve the same sort of risk transfer that BAA has shied away from. “The trouble is these deals haven't always worked,” says Mr Glaister. “Policy and political risks can't easily be transferred and tend to fall back on the state.”

Others are more cautious. Alan Tyler at the University of Loughborough says that Terminal 5 alone will not be enough to convince others that the model ought to be copied. “We'd need to see a few more examples of this working to be sure,” he says. He points out that similar agreements would need a savvy client who can keep a close eye on what contractors are getting up to—something that the government is not famous for.

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Gangmasters

Meals and wheels

Aug 18th 2005
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A murky corner of the labour market is bigger than anyone thought

GANGMASTERS are a vilified bunch who provide a necessary service: putting cheap temporary labour in touch with agricultural demand. The government is trying to regulate them, and supermarkets want to ensure that they do not fill their suppliers' factories with illegal workers. But efforts at reform have been held back by a lack of information on how many gangmasters exist and how many warm bodies they provide. A new study by Precision Prospecting, a consultancy, for the Department for Environment, Food and Rural Affairs indicates that the gangmasters and their employees play a much bigger role in the edible economy than was previously thought.

People who pick lettuces are hard to count. They move around a lot and their work is seasonal, which means that a snapshot of workers on a particular day can be misleading. According to the census of the agricultural labour force in 2003, for example, 63,000 casual workers are employed in agriculture. Jennifer Frances, a Cambridge University economist who is one of the authors of the study, reckons that number is way out. Using data from over 2,000 interviews with businesses in the food production industry, the report estimates that food producers draw on a pool of between 420,000 and 611,000 temporary workers. That's twice the number of people who work for Tesco, Britain's biggest supermarket. The majority are supplied by gangmasters.

Not only is the industry bigger than anybody thought, but it also seems to be growing. Why are the gangmasters flourishing? First, supermarkets have shortened their supply chains. Spare inventory stays in the fields, rather than being stored in the back of the shop. If demand for a product increases suddenly, more workers are taken on to pick, wash, chop and package the ingredients. If demand for Caesar salad wilts, they get laid off.

Second, the growing appetite for convenience food means ingredients are chopped and cooked by workers in factories, rather than at home. That means more work for the packhouses. “There is so much business around that we can walk away from jobs,” says Tony Davies of Provista, a labour provider. The downstream part of the food industry relies heavily on immigrants for temporary labour: nine out of ten workers are not British citizens.

Gangmasters still provide the same essential service to labourers that 19th-century gangmasters did—transportation. Writing of the same Lincolnshire fields where the labour gangs still toil, Karl Marx noted a shortage of cottages, meaning that “labour had to come from open villages, miles away, by long roads that wound along the sides of the hills.” These days, it is driven in from as far away as Scotland.

The government wants to bring all of this activity under its regulatory control. But its sheer size will make that hard, especially since the study indicates that only 52% of temporary workers stay with a labour provider for longer than a month. Gangmasters fear that regulation may increase the cost of doing business legitimately and provide a boon to unscrupulous operators. Perhaps it would be more effective to subsidise cookery classes.

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Prostitution

Massaging the figures

Aug 18th 2005
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The taxman investigates Britain's brothels

ONCE upon a time, the biggest worry for brothels was the police. But the law has increasingly been turning a blind eye to the business. In 1990, there were 140 convictions for brothel-keeping. In 2002, there were fewer than 10. But those who service the nation's sexual needs have a new enemy to deal with, regarded by many as just as alarming as the police: the taxman.

Ruth Morgan-Thomas, of the Scottish Prostitutes Education Project, says she has received many panicky calls from women in Edinburgh and Glasgow worried about tax probes this year. George McCoy, author of *McCoy's Guide to Adult Services*, the definitive guide to British houses of ill repute, says raids in Brighton, Manchester and Leicester signal a new, tougher approach.

The trials of “Barry”, a parlour boss in Oldham, are typical. “I made a deal with the Revenue ten years ago, and have always paid my tax since,” he says. “But this year the ‘shadow economy team’ arrived at my door, wanting the names and addresses of my workers.”

The business models of these barely disguised bordellos explain the unexpected interest. Selling sex is not strictly illegal in Britain. But other, related, activities such as brothel-keeping are. Parlour owners get round this by not employing anyone. They make money by charging entrance fees to punters and nightly rents to their workers. Sexual services are then negotiated privately in small, dimly lit rooms. And while the women who work in the parlours ought to register as self-employed and start paying taxes, a mix of self-interest, ignorance and stigma means most don't.

Industry e-mail lists are alive with rumours of inspectors trawling parlour websites, or tracking the purchase of condoms as a proxy for taxable income. The taxmen deny that their inquiries have been so imaginative, saying that any visits are just part of their 30,000 yearly investigations.

But 500 parlours and roughly 5,000 women adds up to a lot of lost tax money. And so HM Revenue and Customs is firm: “They make money. They should pay tax,” says a spokesman. “The nature of what they do doesn't remove them from their financial obligations.” Faced with new costs, working women will have to redouble their efforts.

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Germany's election

Let battle commence

Aug 18th 2005 | CHEMNITZ AND DRESDEN
From The Economist print edition

Reuters

Gerhard Schröder may still be the loser in next month's election—but it is no longer so certain that Angela Merkel will be the winner

IS THIS really the look of a loser? Stumping in Dresden this week, with the Semper Opera behind him and more than 5,000 spectators in front, Chancellor Gerhard Schröder is not just going through the motions. “We have to reform our welfare state”, he thunders, “or it won't be there for future generations.” Surprisingly, he gets more cheers than boos.

Meanwhile, in the square in Chemnitz, an hour's drive west of Dresden, the crowd of some 3,000 is more excited. But Angela Merkel, the leader of the Christian Democrats (CDU), seems strangely defensive. Instead of giving a broad outline of her policies, she gets bogged down in details: her planned two-point VAT increase won't raise prices across the board because rents, for instance, would be exempt.

In short, as Germany's election campaign began in earnest this week, it was Mr Schröder who was regaining his old spark, while Ms Merkel was looking weaker. The CDU and its Bavarian sister party, the Christian Social Union (CSU), are bickering. The new Left Party remains strong—it is even appealing to far-right voters. Meanwhile heavyweights in the Social Democratic Party (SPD) are jostling for jobs in a putative grand coalition led by the CDU.

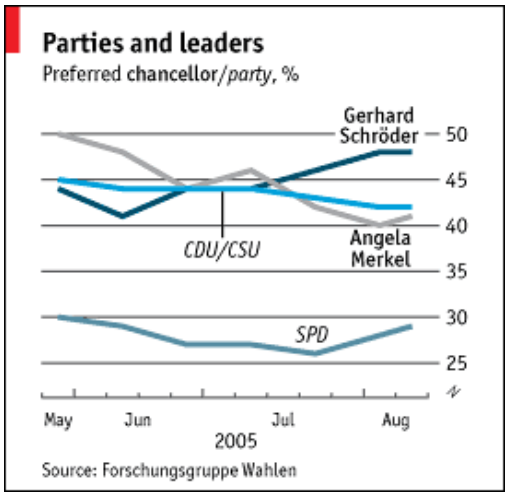
It was always likely that the poll ratings for both Ms Merkel and her party, which hit record highs in late May, would fall. But nobody expected her campaign to get off to such a bad start. Of her programme, voters mainly recalled the plan to increase VAT, which they dislike. Ms Merkel then said that, because of the short campaign, there was time for only one televised debate with Mr Schröder, giving the impression that she is afraid of him. And in an interview, she confused gross and net salaries, damaging for a politician who prides herself on detail.

Yet these mishaps are negligible compared with the harm done by Edmund Stoiber, leader of the CSU. Out of the blue, he started bashing eastern Germans, saying he could not let the east decide Germany's future. “Unfortunately”, he added, “the population is not everywhere as smart as in Bavaria.” Some pundits suggest that Mr Stoiber has still not come to terms with losing to Mr Schröder in 2002. Others argue that he is simply trying to maximise votes in Bavaria, which would increase his influence in a new government. Mr Stoiber's attacks seem sure to cost the CDU votes in the east, and maybe in the west

as well, because people will worry that there will be further infighting if the conservatives win power.

On August 17th Ms Merkel tried to turn the tide with the announcement of a “competence team”, or shadow cabinet. Putting it together was not easy, not least because Mr Stoiber has not said what job, if any, he wants. And the choice of Paul Kirchhof, a former judge on the Constitutional Court, for the finance portfolio may turn out to be not such a good idea. He is a tax expert who favours radical reform, but he has no experience as a politician and his views are at odds with the CDU's programme, not least the plan to raise the rate of VAT.

The biggest influence on the election, though, will be neither Ms Merkel's campaign gaffes nor Mr Stoiber's antics, but the performance of the new Left Party. Before the party was formed from disaffected former Social Democrats in the west, plus the east's ex-communists, Ms Merkel and her would-be coalition partner, the Free Democrats (FDP), were confident of a clear majority over the outgoing SPD/Green coalition, which had lost much leftist support. Now, these homeless leftists have found a new harbour, forcing Ms Merkel to overcome a fully mobilised left.



Yet this does not fully explain the Left Party's 10%-plus poll rating. It is the party of choice for losers from unification and those who think they are suffering from globalisation. But it is also attracting voters who have lost faith in economic reform and in all the mainstream parties. More than two-thirds of the party's potential supporters do not expect any of its programme to be implemented, but most hope it will influence the other parties.

The Left Party may yet win less than 10%. After its novelty wears off, its supporters could discover that it is more populist than truly left-wing. Its joint leader, Oskar Lafontaine, once finance minister under Mr Schröder, excels as a simplifier. When introducing his party's programme, he called for German soldiers to leave Afghanistan to lower the risk of terrorist attacks in Germany. He has also used vocabulary that is usually reserved for the extreme right. Indeed, thanks to the strength of the Left Party, the neo-Nazi National Democrats seem now to have little hope of crossing the 5% threshold for getting into parliament.

With Ms Merkel weakened, Mr Stoiber sabotaging her and Mr Lafontaine losing credibility, Mr Schröder is starting to look better. As a formidable campaigner and proven media charmer, he was always likely to improve his opinion-poll ratings. But this is not a recovery like 2002's, when he came from behind to defeat Mr Stoiber. Tellingly, the media are treating him as if he were on a valedictory tour. Even his remarks about not using military force against Iran have caused less stir in Germany than outside (partly because Ms Merkel essentially agrees with him).

More than anything, it is the battle within the SPD over top jobs in a grand coalition that underscores Mr Schröder's status as a lame duck. Peer Steinbrück, a former premier of North Rhine-Westphalia, and Günter Verheugen, a vice-president of the European Commission, are talked of for the economics and foreign ministries, respectively. Might a coalition with the Left Party be an option in a few years' time? Yes, says Klaus Wowereit, who has been mayor of Berlin in alliance with the former communists for several years.

In the weeks ahead some clarity may emerge. Polls will help to assess the damage done by Mr Stoiber—one taken after his remarks suggested that he has hurt Ms Merkel, but not the CDU. The Constitutional Court still has to rule on whether the election should go ahead. (After a hearing last week,

most observers believe that the judges will acquiesce.) And on September 4th, Ms Merkel and Mr Schröder will hold their televised debate.

This debate will shift the campaign into top gear. Almost half the voters, say some polls, will make up their minds only in the final two weeks. The sole certainty now is that the CDU will end up with the most votes (over 40%), so Ms Merkel remains likely to become Germany's first female chancellor. But whether she will govern with the FDP, which, like the Greens, is stuck at around 7-8%, or be forced into an uncomfortable grand coalition with the SPD, is anybody's guess.

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Turkey and the Kurds

Peace be unto you

Aug 18th 2005 | ANKARA AND DIYARBAKIR
From The Economist print edition

The Turkish prime minister paves the way for a deal with the Kurds

AFP

Erdogan in the Kurds' den

Get article background

WHEN Turkey's prime minister came to power some 30 months ago, few expected his mildly Islamic government to resolve the country's knotty Kurdish question. But last week, in a landmark speech in Diyarbakir, Recep Tayyip Erdogan became the first Turkish leader ever to admit that Turkey had mishandled its rebellious Kurds. Like all great nations, declared Mr Erdogan, Turkey needed to face up to its past. He added that more democracy, not more repression, was the answer to the Kurds' long-running grievances.

Mr Erdogan's visit to the largest city in the mostly Kurdish south-east followed ground-breaking talks with a group of Turkish intellectuals, seen by some as mouthpieces for rebels of the outlawed PKK terrorist group. In these talks, Mr Erdogan pledged that, despite a renewed spasm of rebel violence, there would be no going back on his reforms. The Kurdish problem, he said, could not be solved through purely military means.

The opposition is crying treason. “This will inevitably lead to bargaining with the PKK,” fumed Deniz Baykal, leader of the Republican People's Party. Nationalists within Mr Erdogan's own Justice and Development party have also made angry noises. The army has so far kept silent, even though some retired generals have called for the reintroduction of emergency rule in the Kurdish provinces.

The Kurds have been only a little less provocative. Embarrassingly few showed up at Mr Erdogan's rally. Diyarbakir's mayor, Osman Baydemir, later boasted that “we could have bused in a million people had we wanted.” Orhan Dogan, another Kurdish leader, stoked nationalist fury when he told a newspaper that Turkey would have to negotiate with the PKK and that the group's imprisoned leader, Abdullah Ocalan, would walk free one day. Some Kurds saluted Mr Erdogan for his courage, but even they insisted that he must match his words with deeds.

There are encouraging signs that he will. Within hours of returning from Diyarbakir, Mr Erdogan urged media supervisors to allow regional radio and television stations to broadcast in Kurdish. But more needs to be done if Turkey's Kurds are not to be infected by calls for independence by Iraq's powerful Kurds next door. Measures to stimulate the economy of the impoverished Kurdish provinces must be a priority, as Mr Erdogan has acknowledged. That will necessitate also the return of hundreds of thousands of Kurds expelled from their villages by the army during its scorched-earth campaign against

the PKK.

Mr Erdogan's call to put right past mistakes will ring hollow unless the state compensates the Kurds for their losses. The interior ministry revealed this week that only 5,239 of a total 104,734 victims who had applied under a new law for such compensation had been considered, and only 1,190 were to be paid anything. With the deadline for applications past, the programme “is a complete fiasco”, declared Mesut Deger, an opposition Kurdish deputy, who is pressing for an extension.

Lastly, Mr Erdogan must find a way of giving an amnesty to 5,000 rebels, entrenched in the mountains of south-east Turkey and northern Iraq, that is acceptable to Turks and Kurds alike. The PKK was expected this week to announce a suspension of hostilities, to allow such a deal to be done. Should Mr Erdogan come up with a workable pardon, vowed Naci Aslan, another opposition Kurdish deputy, “I will erect his statue, kiss his feet.”

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Poland, Russia and Germany

The burden of history

Aug 18th 2005 | WARSAW
From The Economist print edition

A testy relationship with the two big neighbours

POLAND'S misfortune has been to be sandwiched between two big and often unfriendly powers, Germany and Russia (Poles say wryly that their historical mission is to kill Germans for duty and Russians for pleasure). Modern diplomacy with both is correspondingly tricky.

The latest row is with Russia, where three Poles—two embassy officials and a journalist—have been beaten up within a week. This was in retaliation for the mugging of three teenagers, children of Russian diplomats, late at night in Warsaw. It was an echo of cold-war habits, when any perceived harassment of Soviet diplomats abroad was swiftly matched in Moscow.

The incident in Warsaw seemed sad but unremarkable. But the Russian reaction was extraordinary. An angry President Vladimir Putin went on television to condemn the mugging. The Polish ambassador was summoned to the foreign ministry, which demanded an official apology. “This disgraceful incident cannot be called a coincidence,” said a spokesman. Dmitry Kosachev, head of the foreign affairs committee of the Russian parliament, the Duma, blamed it on anti-Russian hysteria. Another Duma deputy said the attack was facilitated by Polish attempts to revise the history of the second world war.

Poland and Russia certainly see history differently. To most Poles, Stalin's Soviet Union was first a co-conspirator with Hitler's Germany, and then a murderous occupying power. Under Mr Putin, Russia glorifies the Soviet Union's defeat of Hitler, and whitewashes everything else. Newer issues grate too. Some Polish politicians have backed Chechen rebels. Poland strongly supported the “orange revolution” in Ukraine, which Russia resisted. The Poles champion their persecuted ethnic kin in Belarus, whose authoritarian regime is one of Russia's closest allies.

The Russians accordingly see the Poles as ungrateful, meddling American lackeys. This places Poland in a bind. The obvious thing to do is to protest, but that only strengthens Russia's argument that Poland (like the Baltic states) is a shrill Russophobe that is out of line with the rest of the European Union. This argument seems to sway the EU, which regards all the ex-captive nations' rows with their former master as bilateral matters. Germany's chancellor, Gerhard Schröder, in particular, has seen good relations with Mr Putin as more important than Polish neuroses.

That could change if Angela Merkel, the centre-right candidate, replaces Mr Schröder after next month's German election. Ms Merkel was in Warsaw this week, promising that Germany would treat Poland with equal consideration to France and that the EU's eastern policy would not be made over Poland's head. A Merkel win would be good news for conservatives in Poland, whose foreign-policy stance is overshadowed by the savvy ex-communist president, Aleksander Kwasniewski.

But there's a problem with Ms Merkel too. She supports the building of a museum in Berlin to commemorate the expulsion of millions of Germans from her country's eastern territories (now mostly part of Poland) after the war. This is a favourite cause of the German right, but it is anathema to Poles, most of whom think the Germans got what they deserved.

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The media in Spain

Television wars

Aug 18th 2005 | MADRID
From The Economist print edition

The government continues to have too much influence over the media

SPANIARDS have a phrase to describe the attitude of the country's media giants as they await the government's decision on the allocation of digital television licences: "*callarse como una puta*", to shut up like a whore. Why publish a report that may offend the Socialist government of José Luis Rodríguez Zapatero, if it could jeopardise your share of the digital cake? This was what one journalist was told by his bosses when he asked why his report describing Tony Blair's lukewarm reception of Mr Zapatero's plan to cure the ills of Islamic radicalism through an "alliance of civilisations" had not been published.

In a country whose bestselling newspapers are mostly football-oriented, it is the all-powerful television that really matters. Mr Zapatero's government has caused considerable upset by appearing to lean too far towards the leftish Grupo Prisa, run by Jesús Polanco. The group, which owns the newspaper *El País*, runs the country's only analogue pay-television channel, Canal Plus, through its sister company, Sogecable (this monopoly arose from a licence given by a previous Socialist prime minister, Felipe González). Until the analogue shutdown and conversion to digital, planned for 2010, the government will allow Canal Plus to broadcast without the requirement for a set-top decoder, with the exception of a few high-value programmes such as football coverage.

Competitors complain that this will enable Sogecable to gain an unfair advantage, because it will have a chance to win a much bigger audience before the analogue shutdown, while still maintaining its existing subscriber base. In what seems sure to be an overcrowded field, the government has hinted that it will grant two digital licences apiece to the existing broadcasters (Sogecable, Telecinco, Antena 3, Veo TV and Net TV); another to an analogue station yet to be granted a concession during the transition phase; and a further two licences in 2010.

The government has presented the plan as essentially neutral and technical, but the centre-right opposition People's Party (PP) is concerned that Grupo Prisa is in fact becoming an unassailable force in the radio, television and newspaper market. As the PP knows from its own experience, political control of the media is a vice that is hard to kick. Only last week, the PP president of the Madrid region, Esperanza Aguirre, dished out local television broadcasting licences to sympathisers ranging from the Roman Catholic Church to right-wing media barons.

With the private television market being carved up in a predictably partisan way, what of Mr Zapatero's plan to put an end to government interference in state television and radio? It looks likely to fizzle out too. A council of wise men, convened to find ways of creating a more independent operation, has submitted a report. But few have hopes for any great change so long as state television depends on government grants, and its director-general is chosen by a parliamentary committee.

With the argument over digital television licences likely to remain live right up to the next election, due in three years' time, the media will continue to be cautious over criticising the government. And Mr Zapatero, like all his predecessors, will come to seem insincere in his stated ambition of eradicating government influence over the media.

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Georgia and Ukraine

An odd couple

Aug 18th 2005 | TBILISI
From The Economist print edition

Two presidents who should swap jobs

STRUGGLING with a divided government and a fractious parliament, Viktor Yushchenko, Ukraine's president, last week visited Georgia to see his friend Mikhail Saakashvili, whose problems are even worse. Mr Saakashvili, who swept to the Georgian presidency after the "rose revolution" a year before Ukraine's "orange" one, imparted tips on how to govern after an upheaval—and, perhaps inadvertently, how not to.

Georgia and Ukraine share two characteristic post-Soviet difficulties: endemic corruption and Russian meddling. In both areas, Mr Saakashvili has scored some successes. Russia has dropped its preposterous conditions for leaving its remaining military bases in Georgia (its Black Sea fleet is still based in Ukraine's Crimea), agreeing to be out by 2008, a reversal of policy that Mr Saakashvili attributes partly to American pressure. But in other respects, the Russians are irking Mr Saakashvili more than they are Mr Yushchenko. A porn film, depicting a supposed mile-high tryst between Mr Saakashvili and Yulia Timoshenko, Ukraine's prime minister, captures a prevalent Moscow attitude to its disloyal former vassals.

Mr Yushchenko has only to contend with the enduring suspicion of Russophone eastern Ukraine. Mr Saakashvili faces Russian sponsorship of Abkhazia and South Ossetia, two breakaway Georgian enclaves. The Georgians believe that Russians were involved in a bombing in Gori in February: Mr Saakashvili says he hopes it wasn't the federal government. Both Georgia and Ukraine are vulnerable to capricious spikes in Russian gas prices; both want to diversify energy supplies.

On corruption—a big issue in both revolutions—Mr Yushchenko has muddied his reputation by angrily rebuffing questions over his son's mysteriously extravagant lifestyle. But he has also emulated Mr Saakashvili's anti-corruption strategy of wholesale sacking and prosecutions, even if critics say some punishments look like vendettas. In Georgia, the strategy seems to be working: tax revenues are up as businesses come out of the shadows, and graft-facilitating red tape has been cut. Mr Saakashvili is dispatching Kakha Bendukidze, his principal tape-cutter, to help do a similar job in Ukraine.

Another problem that Mr Saakashvili can advise on is the post-revolutionary let-down. He says he is over the "expectation crisis" of earlier this year, and has delivered such concrete improvements as better roads, more trustworthy police, education reform and more reliable power. But his critics say he has focused too little on the tough business of the economy and too much on symbolic triumphs and stunts, such as his Ajaria adventure (see article), Russian bases and the idea of a new block of democracies that he and Mr Yushchenko proposed last week.

This concern for public relations is an aspect of what some say is his biggest failing: his tendency to behave like a revolutionary, trusting only a few loyalists, disliking criticism and valuing ends above means, as in some of the questionable methods used in his early anti-corruption push. Zurab Zhvania, his prime minister, was said to be a restraining influence on the president's impetuosity. But he died in February. Mr Saakashvili has bolstered the presidency's powers; his party has a huge parliamentary majority; and he has no serious rivals. The biggest protests against his government came after two popular wrestlers were jailed for extortion. The president says that the country's critical media compensate for the opposition's weakness; some complain that they are tame.

By contrast, the cerebral Mr Yushchenko may be too unrevolutionary. Even during the revolution he was hardly rabble-rousing, and he has not been able to discipline his government into coherent policy-making. He is due to give many of the president's powers away in a constitutional reform—a mistake, says Mr Saakashvili: he "should at least keep what he has." If they could borrow each other's personalities for a while, they might both do better. Time for a presidential job swap?

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Georgia's breakaway enclaves

After Aslan

Aug 18th 2005 | BATUMI
From The Economist print edition

Ajaria, a Georgian success story

Get article background

"FOUR minutes," says Levan Varshalomidze proudly, as a car zips across what was once a frontier between the Soviet Union and NATO, and is now the border between Turkey and the republic of Ajaria in Georgia. Under Aslan Abashidze, Mr Varshalomidze's predecessor as Ajaria's boss, the crossing often took an hour and several bribes.

Mr Varshalomidze bears little resemblance to the grizzly strongmen who have usually run mini-fiefs in the Caucasus. A young protégé of Mikhail Saakashvili, Georgia's president, he was installed after street protesters had forced Mr Abashidze, who ruled Ajaria as a quasi-independent state, to flee to Moscow last year. Where Mr Abashidze was habitually accompanied by a phalanx of black-clad toughs, Mr Varshalomidze strolls around Batumi, Ajaria's capital, with a lone bodyguard.

Even more than the rest of impoverished Georgia, sub-tropical Ajaria ought to be prosperous. Mr Varshalomidze talks wistfully of times before the Russian revolution, when Batumi had 18 foreign consulates. To recapture its lost glory, he plans a clutch of new hotels, with perhaps a golf course on the site of a big Russian military base, which the Russians are quitting. Failing state-owned enterprises will be privatised for nominal sums. There will be a new dolphinarium, the dolphins having been lost from the old one.

Mr Saakashvili needs Ajaria to prosper as an incentive to Georgia's two remaining Russian-backed breakaway regions, Abkhazia and South Ossetia. Both fought their way to de facto secession in the early 1990s (refugees from Abkhazia's war still live in high-rises on Batumi's seafront). Mr Saakashvili has proposed a new reconciliation plan for South Ossetia; but after renewed fighting last year, he is distrusted. Abkhazia this week held Lilliputian but provocative military manoeuvres, and its leader said that almost all its inhabitants would take up Russia's offer of citizenship.

Neither is likely to be impressed by Ajaria's limited "autonomy". Still, Mr Varshalomidze and Mr Saakashvili do seem to have brought some benefits to Ajaria, including a mini-influx of Armenian tourists, who, says Mr Saakashvili, no longer face extortion by the "old, big-bellied traffic policemen" whom he sacked en masse. Visiting Batumi this week, Mr Saakashvili took a chaotic stroll along the seafront and opened a cinema, co-opting a photogenic child to cut the ribbon. "Is there popcorn?", he demanded of Mr Varshalomidze.

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Property rights and eminent domain

Hands off our homes

Aug 18th 2005 | ARDMORE, PENNSYLVANIA
From The Economist print edition

A Supreme Court ruling that allows the government to seize private property has set off a fierce backlash that may yet be as potent as the anti-abortion movement

IF YOU ever doubted the importance of the Supreme Court, consider the fuss about *Kelo v New London.* The five-to-four ruling by the court on June 23rd, apparently giving the government the power to bulldoze homes on flimsy grounds, has set off fiery protests across the country.

Americans used to believe that their constitution protected private property. The Fifth Amendment allows the state to seize it only for "public use", and so long as "just compensation" is paid. "Public use" has traditionally been taken to mean something like a public highway. Roads would obviously be much harder to build if a single homeowner could hold out forever or for excessive compensation. The government's powers of "eminent domain" have also been used to clean up "blighted" slums.

Kelo was about something different, however. A private developer in New London, Connecticut, wanted to raze some perfectly nice waterfront homes to build an office block and some posh apartments. The owners didn't want to sell. The city decided to force them to, calculating that the new development would create jobs and yield more taxes.

The Supreme Court took the city's side. Rejecting "any literal requirement that condemned property be put into use for the ...public", Justice John Paul Stevens said it was enough that the seizure should serve some vaguely defined "public purpose"—such as those new taxes. This had nothing to do with slums or roads: instead, it massively expanded the government's power of eminent domain.

The backlash began immediately. Dissenting justices such as Sandra Day O'Connor (who retired last month) pointed out what extraordinary powers the court had just granted the government. "The spectre of condemnation hangs over all property," she wrote. "Nothing is to prevent the state replacing any Motel 6 with a Ritz-Carlton, any home with a shopping mall, or any farm with a factory."

If people can be evicted to make way for others who might pay more taxes, added Clarence Thomas, the court's only black justice, it is not hard to predict who the most likely victims would be. "Urban renewal", he noted, has sometimes been nicknamed "negro removal".

Seven days later, by a ten-to-one margin, the Republican House of Representatives passed a motion disagreeing with the court. A constitutional amendment to overrule *Kelo* is before the House, while a bill

that would have a similar effect is before the Senate. Delaware, Alabama and Texas have already passed laws restricting the government's power to grab private property. Legislators from two dozen other states have either proposed similar bills, or promised to do so.

Meanwhile, a grass-roots movement has arisen to keep other people's hands off private homes. Libertarian groups such as the Institute for Justice, which were campaigning against eminent-domain abuse before *Kelo*, report an upsurge in support, both moral and monetary.

Property grabs on behalf of private developers have been common for some time: the Institute for Justice documented some 10,000 threatened or actual cases between 1998 and 2002. Several cities, including New York, claim that without eminent domain they could never have cleaned up their shabby centres; you could not have created the big spaces that modern retailers wanted at Times Square without forcing small shops to sell.

Since *Kelo*, the law may have shifted in favour of the men with the bulldozers, but public opinion has swung sharply the other way. Polls suggest that 90% of Americans disapprove of the kind of seizures allowed by *Kelo*. Such is the anger that some developers say they are shunning even the kind of eminent-domain seizures that would have been legal before *Kelo*.

Property-owners fighting against local government have been buoyed by the backlash. In the town of Ardmore, Pennsylvania, for example, a small group of businessfolk received letters last year informing them that their shops were to be demolished to make way for a new development including apartments and a parking garage.

Their story is typical of the cavalier fashion with which eminent domain has been used, even before *Kelo*. Ardmore is part of the township of Lower Merion: its board of commissioners had decided that Ardmore's central thoroughfare needed sprucing up. They had some federal funds to build a new railway station, and they decided it would be nice if more commuters could live nearby so they could walk to the station. But instead of offering to buy out the people whose businesses would have to be demolished, they simply told them they would have to move.

“It was devastating,” says Eni Foo, whose Chinese restaurant is on the list. “I've been in the United States since 1963. I came as a graduate student and stayed because I love America. I always believed America [respected] individuals' rights.”

The local government had declared the area “blighted”. But a brief walkabout reveals that it is no more blighted than the potato you ate for lunch. A couple of shop fronts are a bit tatty, but otherwise it looks fine. Indeed, the district has been officially designated “historic”, since much of it was built in the 19th century. The condemned properties include a second-hand shop that supports the local hospital, a club for veterans of foreign wars and Scott Mahan's stationery shop, which has been in his family since 1926.

“I'm not an activist,” says Mr Mahan, “but the more I read about it, the angrier I got. If they were going to do it the American way, they'd negotiate with everyone until everyone was happy. But using eminent domain is totally different.”

Mean streets

Those who are uprooted under eminent domain must be given fair compensation. But if they have no choice but to sell, it may be hard to determine what a fair price for their property is. Developers who know the sellers have to sell will surely be tempted to “lowball” their offers.

The question is not whether the development plan is good or bad. (Some say it will make Ardmore prettier and less congested; others that it will make it uglier and more yuppified.) What matters is whether the plan represents such a pressing public good that it is reasonable to use the state's vast coercive power to execute it. For most Americans, Interstate-95 passes muster, but yuppie condos don't.

The merits or otherwise of the Ardmore plan have been obscured by the protests it has provoked. The “Save Ardmore Coalition” now has 1,000 members—not bad for such a small town. Its members have linked up with national groups such as the Institute for Justice. And since *Kelo*, state and national politicians have started to take an interest. The Pennsylvania legislature is considering a bill to curb the abuse of eminent domain. Mr Mahan is going to testify.

Lower Merion's board appears to be retreating. Matthew Comisky, its president, admits that it was a

mistake to send out those letters summarily telling shopkeepers they were to be evicted. He says that no final decision has been made as to whether to invoke eminent domain. The plan must first undergo an environmental audit, he says, and the board will not be able to vote on a final plan until next year. He denies that the protests have prompted the board to change tack, but admits that the protestors "have done a good job of publicising themselves."

Small-government conservatives hope that *Kelo* will prove to be a tipping point. "Twenty years from now, people will look back at *Kelo* the way people look back at *Roe v Wade* [the 1973 Supreme Court decision that barred the states from banning abortion]," says Grover Norquist of Americans for Tax Reform, a lobby group.

Before *Roe*, state legislatures were legalising abortion one by one, without provoking much protest. *Roe* galvanised pro-lifers by suddenly making (fairly unrestricted) abortion legal everywhere in America, and by doing so in a way that many still regard as illegitimate. The majority judges decided that the constitution contained a "right to privacy" which, though not mentioned anywhere in the text, allowed any woman to abort her foetus in the first trimester.

The *Kelo* ruling was less convoluted, but its opponents think it equally unconstitutional. Mr Norquist calls it both "outrageous" and "manna from heaven", since the property-rights movement it spawned will be at least as electorally significant as the anti-abortion movement. It will be worth 3-5% of the vote, he predicts.

Meanwhile, it has trebled Mr Comisky's workload. Since he also has a full-time day job as a lawyer, this means he hardly sees his family. "Last night I put my son to sleep at 9pm and got up 3am," he says. He adds that he will not seek re-election when his term expires.

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The budget deficit

Cocktail-bar calculations

Aug 18th 2005 | WASHINGTON, DC
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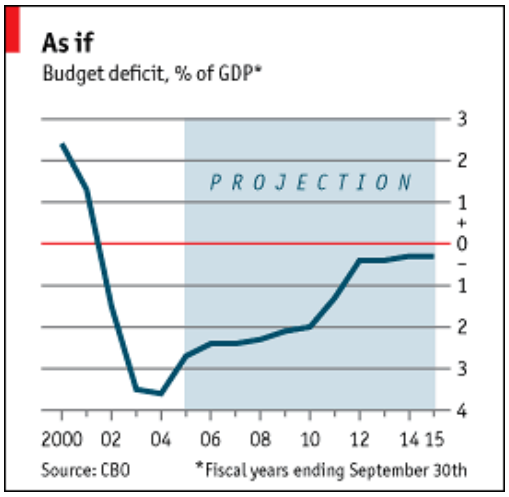
Are George Bush's tax cuts paying for themselves?



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NOT many economists find fame in a cocktail lounge. But it was in just such a venue that Arthur Laffer in 1974 drew the “Laffer curve” on the back of a convenient napkin. The sketch, still more popular with politicians than economists, illustrated how lower tax rates, by spurring growth, might leave tax revenues undiminished. Tax cuts might pay for themselves.

None of the weighty studies produced by the Congressional Budget Office (CBO) would fit on the back of a napkin. But the latest projections from the legislature's non-partisan budget-watcher have excited a few of Mr Laffer's fans. The federal budget deficit, the CBO reckons, will narrow to $331 billion this fiscal year (which ends on September 30th), from $412 billion the year before. Tom DeLay, the Republican majority leader in the House of Representatives, was quick to offer a Laffer-like explanation: “Lower taxes and spending discipline spur economic growth, which in turn cuts the deficit,” he opined.

In fact, spending discipline is still rather lacking. Government outlays will increase by $181 billion (or 8%) this year, a figure that does not include the cost of the pork-stuffed highway bill, signed by the president on August 10th. The fall in the deficit owes rather more to the other side of the ledger: tax revenues are set to grow by $262 billion, or 14% this year. They will increase as a share of GDP for the first time under this tax-cutting president.

Income taxes withheld from pay cheques account for some of the new revenues, but many of the gains are in more exotic areas. The government's take from such things as capital gains, payouts from pension funds, and “sole proprietorships” (one-man companies) should increase by 28% this year, the CBO reckons. Corporations are also making a strikingly handsome contribution to the state's coffers, paying $80 billion (or fully 42%) more than the year before. A third of this bounty seems to be due to the demise of a corporate tax break, which allowed firms to deduct up to half their investment costs from their taxable profits last year. But some $53 billion of it caught the CBO unawares, and remains unexplained.

Is Mr DeLay right to attribute any of these gains to the seductive curves of supply-side economics? In December, Gregory Mankiw, who used to be chairman of Mr Bush's Council of Economic Advisers, and

Matthew Weinzierl, a colleague at Harvard University, published a “back-of-the-envelope guide” to tax rates and revenues. Given the relatively low tax rates prevailing in America, they thought that tax cuts could not be entirely self-financing. But by their reckoning cutting taxes on labour would generate enough growth to recoup about 17 cents on the dollar, and a tax cut on capital could pay for more than half of itself. The government would take a thinner slice of a bigger pie.

Left out of these calculations is any guide to what happens when taxes are cut but spending is not. The budget deficits that ensue will tend to “crowd out” investment, slowing growth. The CBO calculates that every extra dollar of federal borrowing reduces investment in the economy by 36 cents.

The White House, according to its latest forecast in July, now expects to leave a deficit of $162 billion by the time the president leaves office in 2009. But it assumes (absurdly) that Congress will not add a single dollar to its discretionary spending on anything except defence and homeland security from 2006 to 2010. It also leaves out of its projections any extra money for Iraq, Afghanistan or the war on terror.

The CBO makes the opposite assumption. It assumes that by 2009, all of these missions will remain far from accomplished, costing the American taxpayer the same amount, in real terms, as they do today. Partly as a result, the CBO shows Mr Bush bequeathing a deficit of $321 billion to his successor.

Though the CBO's outlook is substantially worse than the White House's over a five-year horizon, it improves dramatically over ten years. This is not because of some long-run Laffer curve; but because the CBO assumes that Mr Bush's tax cuts will expire, as scheduled (the bulk of them in December 2010). That looks extremely unlikely: no politician would allow it and Mr Bush is already trying to make them permanent. If that happens, it would add $349 billion to the deficit in 2015, plus an extra $83 billion in debt service costs.

The CBO's job, says Douglas Holtz-Eakin, its director, is to forecast the economy and the budget, not Congress. It is required by law to assume that Congress will carry on doing what it currently does, adjusted only for inflation. “Everything we have presented today is going to be wrong,” he confidently predicted as he unveiled his report. The same, of course, could be said of Mr Bush's projections.

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Social Security

Seventy years of plenty

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AP

An anniversary to ponder

“THE civilisation of the past 100 years, with its startling industrial changes, has tended more and more to make life insecure. Young people have come to wonder what would be their lot when they came to old age. The man with a job has wondered how long the job would last.”

Not the words of a present-day worrier, wringing his hands about globalisation, but those of President Franklin D. Roosevelt upon signing the Social Security Act into law, 70 years ago this week. The venerable public pension system famously sought to give some measure of protection against these “hazards and vicissitudes of life”.

It started levying taxes on workers' wages in January 1937. It collected a nickel from one Ernest Ackerman on its first day of operation and then paid him a lump sum of 17 cents on his retirement the next day—an enviable rate of return never since repeated. From 1940, participants could claim a monthly benefit from the age of 65 until death.

Back then, life expectancy at birth was only 58 for men and 62 for women. Even after you had survived childhood and started to contribute to the programme your chances of living to see a benefit cheque were not much better than evens (54% for men; 61% for women). Today's retirees, of course, collect far more cheques. By Social Security's 90th birthday, the payouts will cost 110% of the contributions. Unsustainable? No doubt. But reforming Social Security poses its own “hazards and vicissitudes” for politicians, as George Bush is finding out.

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Miami

From coke to cubists

Aug 18th 2005 | MIAMI
From The Economist print edition

And the condos keep on selling. For the moment

NOT for the first time, Miami is being rebranded. Hollywood is at work on an upmarket movie version of the 1980s TV series, “Miami Vice”. Crime is down, employment up and the city's boosters claim outsiders are being lured to South Florida for its new cultural attractions as much as its sun-and-sin pleasures.

As if to complete its transformation from drug-dealers' playground to mainstream metropolis, Miami also has an all-American property boom. Last year, the tax roll in Miami-Dade County grew by 16.5%—the biggest jump for 30 years (and also the third year of double-digit growth). The city of Miami's property-tax base rose a staggering 27% in 2004. House prices have doubled since 1999.

About 65,000 condominium units are either under construction, approved for building or in some stage of the permit process. Most of these condos are in Miami's long neglected downtown area. A small studio apartment can cost $200,000; the posher developments, with names like Icon, Onyx and Nirvana, throw champagne parties for prospective buyers to inspect the marble-packed kitchens, fancy spas and waterfront views.

Unsurprisingly, Miami finished top in a study of “mega metro bubbles” by Merrill Lynch, a stockbroker. The Centre for Housing Policy has also given warning that the ratio between income and house prices is growing at an alarming pace in South Florida. Miami has known busts before: in the 1980s the city's Brickell banking district overheated and prices collapsed. Brickell has since bounced back, with several elegant new glass towers and luxury hotels.

The main debate this time centres on how many of the buyers are speculators, either trying to make a quick return or buying to rent (and doing both on borrowed money). “Flipping”—buying and selling condominiums before they are built—rivals beach volleyball as a local leisure sport.

Optimists, a group that includes many city bureaucrats, say all this bubble talk is exaggerated. Johnny Winton, a city commissioner and property developer with a decent record of avoiding previous crashes, points to “a confluence of events that may just make this boom sustainable”. Florida is booming:

sales-tax revenues for the state rose by 11% last year. The economy is also much more diversified: trade now accounts for half Miami-Dade County's GDP and tourism has jumped.

Miami's reputation for crime, corruption and hurricanes, which lay behind much of the white flight of the 1980s, has also been reappraised. The city has been cleaned up, the hurricanes have missed and the summers, though scorching, are much less humid than in cities further north. Meanwhile, Latin America's various woes continue to generate buyers for Miami property. One in three new homes in South Florida is sold to a foreigner.

This boom is also different from its predecessors. Miami Beach, the traditional home of beachfront condos, is already “built out”. Meanwhile, there is not much room left out west, where the city is hemmed in by the (now protected) Everglades. So the city is growing skywards. The 74-floor Met 3 in central Miami will be the tallest residential building south of Manhattan. In many ways that is what Miami needs, say developers. The city has long been a sprawl with little urban planning and a poor public-transport system.

And all those new museums and art galleries are making a difference. In one stretch of Biscayne Boulevard, dubbed the “Miami Arts District”, some 25,000 condos are being built at a cost of more than $1 billion. Many of the buyers are wealthy New Yorkers and other east-coast snowbirds, drawn by the prospect of a busy cultural calendar to accompany Miami's fine winter weather. The city is home to the biggest art fair in the United States and a new $400m Performing Arts Centre is due to open in 2006. “Right now, people are recognising that this is serious,” says Bonnie Clearwater, the chief curator at the Museum of Contemporary Art.

Public funding for the arts in the city has quadrupled in the past five years; private donors have also ploughed money into cultural projects. “Now is the time to take our rightful place as one of the world's greatest cities,” said Miami's mayor, Manny Diaz, in his annual state-of-the-city speech. That is a fair tribute to a place that has put a lot of effort into smartening itself up. But even the world's greatest cities can have property crashes.

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The September 11th attacks

Voices from Ground Zero

Aug 18th 2005 | NEW YORK
From The Economist print edition

AP

What the firefighters and paramedics actually saw that day

AN ARCHIVE of oral history interviews and radio logs released by New York's fire department adds an almost unbearable level of detail to the tragedy of September 11th through the recollections of 503 firefighters and emergency medical staff working at the devastated World Trade Centre site. The interviews were conducted a few weeks to a few months after the attacks.

Many of the rescuers recalled the spectacle of those who jumped to their deaths. Mark Mazur, an emergency medical technician, drove into Manhattan after seeing on television that an aircraft had struck the first tower. From five miles away, “you see these little Xs coming off [the tower]. You say ‘What the hell are these things?’ You're thinking, then, ‘These Xs are people coming off.’”

Mary Merced, another emergency medical worker, was at the site. “I look, I see debris drop, and I look and it was people,” she said. “I could tell you almost every colour clothing all the people that I saw fall had on, how they fell, if they tumbled, if they swan-dived.”

According to Fire Marshal Steven Mosiello, “They were hitting at a rate of probably one every 30 or 40 seconds on to the glass atrium that was there [outside One World Trade Centre], which is a distinct explosion-type sound when they hit...After you saw enough of them you just stopped looking, you knew what it was.”

Captain Mark Stone survived the collapse of the first tower by ducking into an underground garage, but the shockwave and debris caught him. “We just got thrown,” said Mr Stone, “and everything went black and it was almost silent. Right at that moment I saw my two kids, I saw my father who passed away. I was actually in the air flying along and it was only, I guess, maybe a second, and I said to myself, my God, that's it, it's over, because it was black and it was silent.” When the second tower fell, he was caught by more dust: “I was just sort of in a daze. Two 110-storey buildings fell on my head, so to speak.”

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Rocky Mountain states

Home on the range

Aug 18th 2005 | SHERIDAN, WYOMING
From The Economist print edition

An energy boom is under way; will it end in another bust?

WHEN the oil price pops above the $60-a-barrel mark, most state politicians groan in agony. Not in the Rocky Mountains. The five core mountain states—Montana, Wyoming, New Mexico, Colorado and Utah—all predict budget surpluses at the end of 2005, and energy prices are fuelling that prosperity.

Last year, energy companies spent $10.7 billion in acquisitions and development in what geologists call the Greater Rocky Mountain Region (GRMR). The value of Colorado's energy production alone hit a record $8 billion in 2004. A fair share of all this ends up in state taxes and royalties. New Mexico recently increased its revenue projections for the next five years by more than $1 billion, largely thanks to oil and gas prices. Wyoming's take from severance taxes and mineral royalties has risen from $650m in 2002 to $1.5 billion in the fiscal year that has just ended (roughly half the cost of running the state).

Around 90% of the investment is going into drilling for natural gas. Geologists call the GRMR, which has 165 trillion-260 trillion cubic feet of natural gas, “the Persian Gulf of gas”. According to Michael Farina of Cambridge Energy Research Associates, the GRMR currently produces 9% of America's natural gas; that figure could double in the next 20 years.

The gas boom is being driven by technology and higher prices, not new finds. For example, the Jonah gas field in western Wyoming was discovered in 1975, and a single well was drilled that generated 300,000 cubic feet per day. But in 1993 new advances in drilling and geophysics uncovered a field with as much as 5 trillion cubic feet.

Not that oil has faded altogether. In 2003, a field containing as much as 1 billion barrels was found in rural Sevier County, Utah—one of the biggest onshore discoveries in the past 30 years (outside Alaska). And oil companies are searching for more. In 2004, Utah's division of oil, gas and mining approved 1,100 drilling permits, a quarter above the figure for 2003 and double 2002's tally.

The best-placed state is Wyoming. It currently produces a third of the GRMR's gas, and is the home of both the Jonah field and a promising coal-bed methane development in the Powder River Basin. It also accounts for a third of America's coal production: the 376m tons it churned out in 2003 was more than the combined total of the next four largest coal-producers (West Virginia, Kentucky, Pennsylvania and Texas). And Wyoming has the nation's most copious uranium reserves.

However, those with long memories in the Rockies are cautious. They remember the hardship caused by the collapse of energy prices in the mid-1980s, which coincided with an agricultural debt crisis. Isolated communities such as Jeffrey City, Wyoming, became ghost towns when uranium prices dropped from $43 per lb in 1979 to $8 in 1992. Coloradans recall “Black Sunday” in May 1982, when Exxon Mobil laid off 2,200 workers at its Colony Oil Shale project near Parachute.

Rose Skinner, mayor of Pinedale, a gas boomtown in Wyoming, doesn't anticipate such a drama. In the 1980s bust, people just walked away from houses rather than deal with the debt. She doesn't think that will happen again. This may be brave talk, but it also reflects the way that the west has changed.

Pinedale, for example, used to be a sleepy ranching town. Now the energy people are fighting for housing with prosperous “spillovers” from chic Jackson Hole. Unlike the settlers of old, these new residents are rich, educated and litigious. Some have reacted sourly on discovering that when they bought their retirement ranch, “split estate law” gave them title just to the surface rights. Unless the new owner has full mineral rights, energy companies can build new roads and make a colander out of a favourite horse pasture.

The battle has got steamy enough for Wyoming to pass a law giving landowners more power in these wrangles. Water, too, has become an issue, especially in coal-bed methane development. Greens and ranchers alike worry about the millions of gallons of water that must be pumped out of each well before a molecule of gas shows up. The White House, panicked by so many Republicans lunging for each other's throats, has set up a Rocky Mountain Energy Council to set an overall strategy for development on public lands.

Some degree of planning seems overdue. Consider Wamsutter, another gas-town in Wyoming. Its population is normally around 260, but now it has to cope with a camp of 400 itinerant workers. The municipality does not get enough money from the state to build the new streets or sewers it needs. “I'd like to plan for the future,” says Bill Hippe, its mayor. “Right now, it's pretty tough.”

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Brazil's ruling party

The fall of the Workers' Party

Aug 18th 2005 | SÃO PAULO
From The Economist print edition

AG NCIA ESTADO

The ruthless pragmatism of José Dirceu (pictured left with Lula in 1990) has left Latin America's largest left-wing party with a severe identity crisis

Get article background

THE fortunes of Luiz Inácio Lula da Silva, Brazil's president, could yet recover from the corruption scandal which has paralysed his government for the past three months. But his Workers' Party (PT) will never be the same again. An internal election next month is likely to see the party turn further left or split—or both. In any event, it seems set for a drubbing from the voters at a general election next year. The PT's move to the centre in the 1990s stirred optimism about Brazil's economic prospects. It is now in jeopardy.

The scandal turns on allegations that PT officials used illicit cash to finance the party's campaigns and to buy the loyalty of congressional allies. They deny this; no prosecutions have yet been brought. But the affair has already toppled José Dirceu, the president's chief adviser, along with the PT's entire leadership. It has also implicated a score of congressional leaders from the PT and allied parties, along with some opposition figures.

On August 11th, Duda Mendonça, a publicist who orchestrated Lula's 2002 presidential campaign, admitted that he was paid through offshore accounts—a crime if the PT authorised the transaction. For the first time an opinion poll has predicted that Lula would lose next year's presidential election to José Serra, the man he beat in 2002 and who is now mayor of São Paulo. Even so, Lula is not finished yet. He is more popular than his party. There is no proof that he endorsed illegal payments. The economy is set to grow strongly next year. Opposition parties downplay talk of impeachment.

But for the PT, which claimed a monopoly on ethical politics in Brazil, the scandal has precipitated an identity crisis. The party's origins lie in mass strikes which helped to end Brazil's 1964-85 dictatorship. Its election victory in 2002 was widely seen as a sign that Brazil had completed its transition to democracy. The PT's conduct in office appeared to confirm that party and country were maturing together. Like Britain's Tony Blair, and unlike traditional Latin American leftists, Lula's government has made economic stability the foundation of his quest for social justice.

Lula's victory and the pragmatism that followed were made possible by a transformation of the party engineered a decade ago by Mr Dirceu and his allies (known as the “majority camp”). This turned a party of militants—a mixture of Catholic activists, left-wing intellectuals and union leaders—into a mass party of 840,000 individual members. With that came a change in ideology. In its early days the PT knew that it was against capitalism and “bourgeois” democracy, but not what it was for. “We were born saying No,” said a former party leader last year. By 2002, Lula stood for moderate social reform.

But the changes opened up fault lines which the scandal has widened. According to his critics, Mr Dirceu, a former communist who trained as a guerrilla in Cuba, never lost his authoritarian habits. In the state of São Paulo, the PT's base, Mr Dirceu's disciples “profiled the members in every municipality,” assessing their loyalties and “intimidating those who were not in his circle,” says Rudá Ricci, a PT activist turned sociologist.

Others criticise Mr Dirceu's pragmatism. The drive to “win the election at all costs” and ally with parties of the right “dismantled the ethical and political patrimony of the PT,” claims Ivan Valente, one of 15 left-wing congressmen who this month formed a “free PT” faction, which rejects the party leadership. The party's former treasurer, Delúbio Soares, became known as the “suitcase man”, says Mr Ricci. Mr Dirceu denies knowing of illicit financing and insists that he democratised the party, but by most accounts he wielded near-absolute power over it.

The scandals have triggered a three-way struggle for the party's soul. The left wants to restore its former ideology and structure, as well as its ethics. Mr Dirceu's group is fighting to keep control. The party's new president, Tarso Genro, formerly the education minister, is caught in the middle. The PT is due to elect new leaders on September 18th; after the end of that month, prospective candidates in the 2006 elections can no longer switch parties. By then the PT's new shape will be clearer.

Mr Genro is the candidate of the “majority camp” but has criticised the government's economic policy. His efforts to punish tainted party leaders have been blocked by Mr Dirceu. Candidates from several leftist factions will challenge Mr Genro. They want an end to congressional alliances with centre-right parties and the sacking of Antonio Palocci, the orthodox finance minister, neither of which Lula can afford to concede. Much of the “Free PT” could end up leaving the party.

In theory, the majority that remains would form a more cohesive grouping, more supportive of Mr Palocci's moderate economic policies. Most PT congressmen think these are correct, says José Eduardo Cardozo, who is one of them. If miscreants are punished, the PT“will emerge bleeding but whole,” he says.

Maybe. But it will have trouble finding allies and raising money for next year's election. Even if Lula were to win, most analysts expect the PT to lose up to 40 of its 90 seats in the 513-seat lower house. Such setbacks might rob the party of the confidence to promote unpopular reforms. “The majority camp had a clear political project to incorporate market-friendly reforms into a leftist platform,” says Christopher Garman of Eurasia Group, a consultancy. Now “all these guys have fallen.” The new team will worry more about defending the PT's electoral base, which is urban, unionised and resistant to reform. Brazil will have to wait for a Workers' Party that is both pragmatic and clean.

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Canada

For queen—but for which country?

Aug 18th 2005
From The Economist print edition

Questions about a new governor-general's past

AP

A proud Canadian, she says

TIME was when the Queen of Canada, who lives in Britain, sent an ageing noble to be her governor-general in Canada. Nowadays the job is in the gift of Canada's prime minister. And the selection criteria appear to be governed by political correctness—or at least politics.

The outgoing governor-general, Adrienne Clarkson, had arrived as a child immigrant from wartime Hong Kong. On August 4th, Paul Martin, the prime minister, nominated Michaëlle Jean to succeed Ms Clarkson. She seemed to press all the right buttons. Ms Jean is a young, multilingual, black immigrant from Haiti, and like her predecessor, a former television journalist. Most important of all, she is from Quebec, where support for the ruling Liberals has slumped because of a corruption scandal. Mr Martin denied that this was the reason for his choice, but it looked a shrewd one.

Yet Mr Martin's calculations seemingly failed to consider Ms Jean's position on the great Canadian political question: the independence of Quebec. *Le Quebecois,* a separatist magazine, claims that Ms Jean and her French film-maker husband, Jean-Daniel Lafond, had supported Quebec separatism. Film clips purporting to show the couple toasting the cause then emerged.

The Conservative opposition wants guarantees that Ms Jean is a committed federalist. Mr Martin says she is, and that she was carefully vetted. On August 17th, after several days of silence, Ms Jean issued a statement saying she and her husband were “fully committed to Canada”. Barring further revelations, that may be enough to blunt the criticisms.

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Canada's defence policy

Charging round the block

Aug 18th 2005 | OTTAWA
From The Economist print edition

Military reforms elicit a mixed reaction

AS DEMONSTRATIONS of military prowess go, last month's visits by Canadian troops and then by the defence minister, Bill Graham, to an uninhabited Arctic rock claimed also by Denmark fell firmly into the Ruritanian category. But the planting of a Canadian flag and the erection of an Inuit stone marker on Hans Island, as the rock near Greenland is called, was deceptive. Behind it lies a new toughness in Canadian defence policy.

Canada has long claimed sovereignty over the waters of its Arctic archipelago—a stance contested by the United States. Mr Graham's move provoked Denmark into sending a ship to reclaim the rock. Canada, in turn, is dispatching a frigate to the area to keep an eye on Danish fishermen.

The minister's Arctic foray was followed a week later by a more significant deployment: the first units of a 1,500-strong Canadian task force arrived in Kandahar, one of the least secure parts of Afghanistan, where they will take over leadership of a provincial reconstruction team from the Americans. More such ventures may follow. Paul Martin's Liberal minority government plans to increase annual defence spending over the next five years from its current meagre level of C$13.5 billion ($11.2 billion, or 1% of GDP) to C$19 billion and add another 5,000 troops to the 62,500-strong forces.

They will operate in new ways too. The rise to senior commands of three generals with experience of irregular warfare in Afghanistan and the Middle East has set in motion a revolution in Canadian military thinking. General Rick Hillier, the new chief of defence staff, once headed the multinational ISAF force in Kabul; his chief of strategic planning, Andrew Leslie also served there; while Major-General Walter Natynczyk, who is implementing the reforms, is fresh from a year with American troops in Iraq. He and General Hillier have also both served as deputy commander of the US Third Armoured Corps in Texas.

General Hillier described the mission in Kandahar as being “to confront terrorism right at the face”. It was part of the army's job “to be able to kill”, he declared. Common sense, you might think, but many Canadians prefer their military men to be cuddly peacekeepers. They fear retaliation if their forces become more pugnacious. Mr Martin confirmed that Canada could indeed suffer a terrorist attack; such fears should not cause Canadians to shy away from their duties overseas, he said.

Under the reforms, the army, navy and air force are to be integrated in six regional commands

answering to a single Canada Command headed by an admiral. General Natynczuk says the new structure will allow swift co-operation with reservists and civilians in emergencies such as Ontario's ice-storm of 1998. It also mimics the United States' Northern Command, set up in 2002 for homeland defence. A new expeditionary force will respond to calls to intervene in failed states, while an anti-terrorist special forces unit will be strengthened.

Is all this simply an Americanisation of Canada's forces in the name of “inter-operability”, as some parliamentary critics suggest? The new mantra is the ability to wage a “three-block war” in foreign cities, fighting insurgents while also stabilising restless civilians and providing humanitarian aid. The term was borrowed straight from the US Marine Corps, who used it in the storming of Fallujah in Iraq last year.

General Natynczyk denies that the new thinking comes from across the border. He and his colleagues have learnt a lot from working alongside British forces in places like Cyprus and Bosnia too, he says. General Hillier insists that the approach guiding the reforms has been “Canada first”. So expect some more sabre-rattling in the Arctic next summer.

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Energy in the southern cone

Gas ring

Aug 18th 2005 | SANTIAGO
From The Economist print edition

Chile's search for reliable suppliers

Get article background

OVER the next couple of years Chile is likely to be Latin America's fastest-growing economy, as it was for much of the 1990s. But there is one big potential brake: energy. With little oil or coal of its own, Chile imports two-thirds of its energy, relying especially on Argentina's natural gas. Some $4 billion has been invested in gas pipelines and gas-fired power plants. Until recently, Chile was importing 20m cubic metres of Argentine gas per day. This provided a quarter of central Chile's electricity and almost 60% in the north.

But Argentina's government has frozen the price of gas at home: consumption has soared and investment fallen. Since last year it has imposed unilateral cuts in gas exports to Chile of 20% (and at times 50%). Chile has avoided power cuts, mainly because heavy winter rains boosted hydroelectric output. But it urgently needs more reliable suppliers.

One solution might be Bolivia, which has South America's largest gas reserves after Venezuela. But Bolivia still smarts at Chile's annexation of its mineral-rich coastal territory in a 19th-century war. It refuses to sell gas to Chile.

So Chile is looking elsewhere. First, ENAP, the state oil company, plans to award a contract in October for the supply of liquefied natural gas (LNG) and a $400m re-gasification plant near Santiago. A second, more ambitious, plan is for a single “energy ring” in South America's southern cone which would

incorporate gas from Peru's Camisea field. This would use existing pipelines across the southern cone. It would add at least one more, along the Pacific coast from Peru to Chile.

Mooted at a meeting of Mercosur, the region's putative common market, in June, this plan is gathering momentum. A legal framework for it should be drawn up by the end of the year. One obstacle is Chile's quarrel with Peru over their maritime border. But supply cuts for nationalist reasons would be less likely if they also affected Argentina and Brazil, and the project would include some form of supply insurance.

The bigger question is whether the “ring” is the best design for energy integration. The 1,200km (750-mile) pipeline from Peru to northern Chile could cost up to $1 billion. A possible extension to Santiago would increase demand, but over a distance at which it becomes cheaper to import liquefied gas (indeed Peru might be a supplier for the ENAP plant). Transport costs would make Peruvian gas uncompetitive in Argentina. And Camisea may not have enough gas to supply the southern cone as well as the home market and planned LNG exports to North America.

The main purpose of the “ring” appears to be to coax Bolivia (an observer at the talks) into bigger gas exports. “It's amazing how transforming this into a multilateral issue has cut through bilateral difficulties,” says Rudolf Araneda, a manager of a Chilean pipeline. Bolivia has resumed talks on a second pipeline to Argentina (potentially freeing up more Argentine gas for Chile) which it broke off earlier this year because of political turmoil. The “ring” means that Bolivia would no longer hold all the cards in the southern cone's power game. But much will still depend on Bolivia's presidential election in December.

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Peru's president

The masochist

Aug 18th 2005 | LIMA
From The Economist print edition

How not to reshuffle a cabinet

Get article background

IF SHOOTING oneself in the foot were an Olympic sport, Alejandro Toledo would win the gold medal. As he began his fifth and final year as Peru's president, Mr Toledo had been enjoying a welcome wavelet of adulation. Thanks mainly to a strong economy, his approval rating in some opinion polls had risen to 20%—modest enough, but more than double the figure for much of the past 18 months. Pundits expected the president's popularity to carry on rising in the run-up to an election next April. All Mr Toledo had to do was nothing.

That proved too much for him. On August 11th, he named as foreign minister Fernando Olivera, a close political ally. The appointment of Mr Olivera, an outspoken and erratic muckraker, was greeted with derision. That prompted Carlos Ferrero, the prime minister, to quit, triggering the resignation of the whole cabinet.

Mr Olivera complained that Mr Ferrero, having approved his appointment, betrayed him. He said his party might no longer support the government. In theory, that would leave the president with just 34 votes in the 120-seat Congress. Peruvians blamed Mr Toledo for the debacle: his approval rating halved to 8% in one poll.

But this time the president may recover more swiftly than from his many previous self-inflicted wounds (which range from flip-flopping on privatisations to firing reformers and replacing them with nepotists). On August 16th he named Pedro Pablo Kuczynski, the finance minister, as the new premier. Mr Kuczynski, an experienced liberal reformer, can claim much credit for four years of economic growth, which has averaged 4.6% a year, while also improving the public finances. Mr Kucyznski in turn picked his deputy, Fernando Zavala, as his replacement, while Óscar Maúrtua, an experienced diplomat, became foreign minister.

Mr Kuczynski, whom Mr Toledo had earlier this year half-heartedly proposed to head the Inter-American Development Bank, has presidential ambitions. Polls give him less than 5% support, and Peruvians tend not to vote for members of the country's white financial elite. But next year's election looks wide open, with none of the hopefuls commanding more than 22%. If Mr Kuczynski is to run, by law he would have to resign by October 8th. He might be in his new job for only a few weeks—giving Mr Toledo a new chance to create a crisis out of an opportunity.

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The Gaza pullout

Giving up in Gaza

Aug 18th 2005 | DUGIT AND NITSAN
From The Economist print edition

Reuters

The evacuation of Israel's Gaza settlements has gone faster and less violently than many feared. What next?

DUGIT is a tiny enclave on a low hill overlooking the Mediterranean. To the south, the concrete sprawl of Gaza City swelters in the humidity. Dugit's houses, by contrast, are a multi-hued gaggle of airy mansions built to their owners' tastes. One, with its interior spaces arranged in concentric circles and connected by a spiralling staircase, brings to mind a giant exploded conch shell.

But shells are all that remain. The 17 families that used to live there have taken everything, often even stripping out the tiling and plumbing. In a few days the army will come and raze what is left into the dunes. A poignant sign outside one house reads: “D9 [bulldozer] driver: please leave nothing.” On Tuesday August 16th, the day after Israeli soldiers began handing out eviction notices, Dugit became the first of the Gaza strip's 21 settlements to be completely evacuated. By the time *The Economist* went to press on the morning of the 19th, nine more had joined it, as well as two of the four small West Bank settlements due for emptying, and by the government's reckoning 65% of Gaza's 8,000-odd Jewish settlers had left.

There have been protests and clashes, and many tears from both the evacuators and the evacuees; but the massive, lengthy showdown that many feared has so far been avoided. When the hour has come, most of the settlers have left of their own free will. More trouble has come instead from the 5,000-odd protesters from outside Gaza who had made their way in by various ruses. These protesters, often from the hardline West Bank settlements, are mostly young and—unlike the Gaza settlers themselves, who have families and futures to think of—have nothing to lose from confrontations with the army. Hundreds holed themselves up in two synagogues. But so far their attacks have caused only a few minor injuries, although a settler in the West Bank killed four Palestinians in protest against the pullout.

As a result, the army's predicted evacuation timetable has steadily shortened to a matter of days from the original three weeks. It has helped that Palestinian militants, whether by choice or because the Palestinian Authority (PA) has belatedly managed to assert some authority in Gaza, have suspended their periodic mortar and rocket fire on the settlements.

Soon, then, the focus will shift to the settlers' new living conditions. Since the beginning of August, a growing stream of them has been arriving, dazed, at the new neighbourhoods of “caravillas”, the prefabricated houses set up for them to the north and east of the Gaza strip. Plonked down in rows on

the sand with nary a bush for shade, the new neighbourhoods look not unlike the original Gaza settlements themselves.

In Nitsan, the biggest such neighbourhood, with 350 caravillas already in place and another 100 due, new arrivals are greeted by a small army of young volunteers who help them get installed, and by salespeople offering to put in telephone lines and cable television. For the least affluent, the caravillas are little worse than the houses they are abandoning, though exiles from places like Dugit face a harsh comedown. Eventually, using the compensation allocated by the state, worth some $300,000, they will be able to build more permanent homes. There is a bonus for anyone settling in the Galilee or the Negev, two areas in Israel with large Arab populations where the government wants more Jews to live. Most Israelis, though, will care less about the ex-settlers' troubles than about the disengagement's longer-term outcome. Polls have shown a majority consistently supporting it, but there is also widespread scepticism that it will make Israel safer or bring peace nearer.

That depends, first of all, on whether Palestinian militants resume their attacks, which in turn depends on whether the PA can assert itself in Gaza against challenges from a renegade stream in the PLO, the umbrella organisation for Palestinian parties, and from Hamas, the main Islamist party. The PA's failure to bring Gaza under control would effectively put any peace process on hold, with Israel accusing it of not fulfilling its obligations under the international “road map” peace plan.

Secondly, it depends on Israeli politics. Elections are due in November 2006, and before then both Labour and the Likud will choose leaders. A recent poll showed that Ariel Sharon, the prime minister and the disengagement plan's architect, would lose a Likud leadership race to Binyamin Netanyahu, who recently quit as finance minister in protest at the evacuation. There has been talk of Mr Sharon forming a new party. But Mr Netanyahu looks like a rank opportunist to many Likud voters. If the disengagement and its aftermath pass off relatively quietly, Mr Sharon's stock could rise again.

Labour, meanwhile, faces an equally deep crisis: having had its idea, disengagement, stolen by Mr Sharon, can it recover as a credible alternative to the right? Not unless it firmly sets its sights on a two-state solution, says Ephraim Sneh, a Labour Knesset member. The disengagement has widened the cleft in Israeli society between the “blues”, the plan's largely secular supporters, and the mostly religious “oranges”. The election, says Mr Sneh, will be a vote on what kind of state Israel is to be—an orange one that holds on to settlements, or a blue one that does all it can to leave them.

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Iran's nuclear game

Playing hardball

Aug 18th 2005
From The Economist print edition

And no sign of backing down

Reuters

Ali Larijani, nuclear negotiator

Get article background

IN LESS than a month's time, Iran's new government, which has yet even to be sworn in by parliament, could find itself in the dock at the UN Security Council for restarting nuclear work last week at its uranium-conversion plant at Isfahan. Breaking the seals put on Isfahan by the International Atomic Energy Agency (IAEA), the UN's nuclear guardian, also broke the terms of Iran's agreement last year with Britain, France and Germany to suspend all such dabbling with uranium and also with plutonium, two materials that could be used for bomb-making, while their talks continued. Restarting the plant likewise defied repeated IAEA resolutions, including one passed at an emergency meeting last week, calling on Iran to suspend all such nuclear work.

For a government barely in office, this is giving quick offence. Why take on the world so quickly? And what are the chances now of curbing the regime's presumed nuclear ambitions?

The next diplomatic set-piece will be at the IAEA, whose inspectors will report formally on September 3rd about just what Iran is up to at Isfahan, where yellowcake (uranium ore) is converted into a gas that can later be spun in centrifuge machines to make usable uranium. Iran insists that it has every right under the Nuclear Non-Proliferation Treaty to make uranium fuel for civilian power reactors, and that is all it wants to do. But two decades of lies and evasions uncovered by inspectors leave many governments unconvinced.

After rejecting out of hand a raft of European proposals—including co-operation in other civilian nuclear technologies, as well as improved trade, political and security ties—Iran's president, Mahmoud Ahmadinejad, has said Iran will present some ideas of its own to break the deadlock. Yet its new chief nuclear negotiator, Ali Larijani, appointed at the behest of the country's ruling clerics, insisted this week that uranium conversion will never be stopped; future talks, he said, would concern only the conditions under which Iran will restart work at an enrichment plant it is building at Natanz.

If Iran sticks to its guns, the IAEA's board will reconvene later in September, with little choice but to refer it to the Security Council. There the stance of Russia and China, both veto-wielding members, will be crucial. Indeed, Iran may well be counting on their help. Yet Russia, increasingly worried about Iran's intentions, would likely back an initial resolution calling on Iran to comply with IAEA requests. It could help too, argues Henry Sokolski of the Non-Proliferation Policy Education Centre (NPEC), a Washington-based think-tank, if the IAEA's board or the council were to call for nuclear co-operation with Iran to be suspended until inspectors are certain they have a full accounting of its nuclear past. That would give Russia legal cover formally to suspend its work on Iran's Bushehr reactor.

China then might be loth to cast a lone veto. But the difficulty of getting beyond a wrist-slap from the council explains why the Europeans have been in no rush to get there. By reacting calmly in the face of the crisis Iran has now provoked, they hope to keep it squarely on the spot. Iran's tactics, by contrast, are to force the pace in the hopes of cracking European solidarity, splitting the Europeans from America, and appealing over their heads to those governments chary of setting a restrictive precedent on nuclear fuel-making that could hamper their own nuclear ambitions. Iran's recent intemperate behaviour ought to strengthen the Europeans' hand. Yet the difficulties of keeping even the European three on message are already apparent. Caught up in his own re-election effort, Germany's chancellor, Gerhard Schröder,

broke ranks publicly by ruling out any future military action against Iran (none is planned).

The irritation that caused among British and French diplomats, however, is nothing compared with the difficulty they and America will face if Iran continues to balk. Theoretically, the Security Council could take a whole range of measures to make Iran uncomfortable: from selective visa bans for those involved in its nuclear programme, through embargoes of various kinds, to tough economic sanctions. But there is no consensus on any of these.

The UN is not the only recourse. But for their part the Europeans, unpractised at common coercive diplomacy, are only just starting to think through the ramifications of what might be needed. One idea doing the rounds if diplomacy goes on failing is for a maritime cordon, based on the practice of the American-led Proliferation Security Initiative, to stop shipments related to Iran's nuclear and other weapons programmes: a sort of PSI for the Gulf region. But making such a cordon tight and effective would be hard, especially without full support from Iran's neighbours, argues Michael Knights in a recent paper for NPEC. Meanwhile Iran has already hinted that if push came to shove, it would not be shy of using its own weapons: chiefly its oil and gas, but it also has a growing navy of its own. It shows no signs of blinking first.

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Iraq

More jaw-jaw

Aug 18th 2005 | BAGHDAD
From The Economist print edition

Parliament dithers on

ON AUGUST 15th, barely 20 minutes short of a previous deadline, Iraq's parliament voted to give itself another week to agree on a new draft constitution. Had it not managed to agree to keep talking, the assembly would have dissolved in wretched failure. The postponement, which entailed an amendment to the country's American-approved Transitional Administrative Law (TAL), followed days of optimistic proclamations from politicians that a timely agreement would be reached by the country's main ethnic and sectarian blocs. But as the negotiations proceeded to unravel, such an agreement seemed hard to imagine.

In the weeks before the deadline, a rough consensus had emerged between two of the parliament's three main groups, the Shia Muslims and ethnic Kurds. For the Kurds, America's best ally in Iraq, the new constitution should be mainly based on the TAL—unsurprisingly, seeing as they largely wrote it. Yet they were also prepared to make concessions to the Shia, the country's majority group. Thus, for example, Iraq would remain a federal republic, but its revenues from oil, which is concentrated in the north and south, would be shared among the provinces according to population size.

The Kurds would remain autonomous in their northern redoubt, retaining control over their *peshmerga* militias. Kirkuk, an oil-rich province which both the Kurds and Sunni Arabs lay claim to, would be dealt with according to the TAL: the Kurds deported from the province by Saddam Hussein would be allowed to return, after which a referendum would be held on whether to include it in the Kurdish domain. Islam would meanwhile be the state religion, and the leading role of the Shia clergy acknowledged; but the country would not be run strictly according to Islamic law. Yet, as the deadline loomed, Kurdish and Shia politicians admitted that any number of these points were still under negotiation. And many Sunni rejected them altogether.

The Sunnis came late to the table, after a succession of disputes over how many of—and who among—their representatives would sit on the parliamentary committee negotiating the new draft constitution, as well as a short boycott after two Sunni delegates were assassinated. Moreover, many still cling to the vision of the Sunni-dominated old regime, insisting that Iraq be an “Arab Republic”—a non-starter with the Kurds—and flatly rejecting the notion of federalism. Other Sunni delegates accepted Kurdish autonomy as an established fact, but refused to countenance demands for a Shia-run autonomous region in the south. This, they said, would deprive the mostly Sunni centre of oil revenue, and also allow next-door Iran's Shia rulers to meddle in Iraq's affairs.

Can the Sunnis be brought on board in the next week? Some Shia and Kurds have suggested that they might push through a draft constitution without Sunni support. But, reasonably enough, the Sunnis counter that they would then campaign against the draft when it came before a referendum in October. Under the TAL, the draft cannot be ratified if two-thirds of voters in three provinces vote against it; most likely, four of Iraq's provinces have Sunni majorities. And besides, any bid to steamroll Sunni objections would probably inflame the raging, Sunni-run insurgency.

As the squabbling grows, America has become more involved in internal Iraqi politicking than at any time since it, technically, handed over the country's sovereignty to the Iraqis last year. The American ambassador, Zalmay Khalilzad, has met regularly the leaders of each competing faction, and urged them to reach a consensus as quickly as possible. For them to do so, the Sunnis must accept that they no longer have the strength to dictate their country's course.

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Nigeria's police

When the cops are robbers

Aug 18th 2005 | LAGOS
From The Economist print edition

It will not be easy to clean up the country's police

AP

Your friendly neighbourhood bobby

ON THE streets of Lagos, Nigeria's bustling megalopolis, it is often said, only half-jokingly, that there is less crime when the police are not around. Nigeria's police are well known for extorting bribes from drivers at checkpoints and for their heavy-handed treatment of suspected criminals. Despite the end of military rule in 1999, ill-paid officers are still a law unto themselves, and torture, beatings and extrajudicial killings persist.

A recent report by Human Rights Watch, a lobbying group, quotes police figures acknowledging that policemen killed 3,100 suspected armed robbers in combat in 2003, up from 2,021 in 2002. An increase in the ratio of killings to arrests since 2001 is attributed largely to a deliberate crackdown ordered by the then police chief, Tafa Balogun, dubbed "Operation Fire for Fire". The police anti-riot unit, known as "Mopol" (Mobile Police), so frightens Nigerians that its nickname is "Kill and Go".

So although violent crime still blights Africa's most populous country, attention is turning to disciplining policemen for human-rights abuses. Mindful of a proposed write-off of a chunk of debt by international creditors, and still hopeful of winning a permanent seat on the UN Security Council, Nigeria is keen to transform its image in the world. Last month five Nigerian policemen were taken to court to face charges of shooting dead unarmed civilians on the outskirts of the capital, Abuja. The case is the first of its kind, and the gory details have received saturation coverage in the country's press. "Such procedures need to become routine in such cases if the police are to get the message", said Philip Alston, the UN's special rapporteur on extrajudicial executions, after a recent official visit to Nigeria.

But while the trial of the policemen is encouraging, a proper prosecution will still be subject to the vagaries of Nigeria's cumbersome and corrupt judicial process. And things seem little better at the top of the police force. The long awaited prosecution of Mr Balogun, who has been charged with embezzling around $100m from police funds, is in doubt. He was a key ally of President Olusegun Obasanjo, re-elected two years ago in a poll marred by vote-rigging and violence. He may benefit from a plea bargain.

And despite Nigeria now spending more on its 300,000 policemen than on its armed forces, the attitudes of many of them do not seem to have changed very much since "Operation Fire for Fire" was rebranded "To Serve and Protect with Integrity". "We're dying, and we don't receive proper pay," says a young policeman. "What are you serving to protect, when you are not properly fed? Fire for Fire is best."

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Niger

The worst is over

Aug 18th 2005 | NIAMEY, NIGER
From The Economist print edition

But dreadful problems remain

THE severe food shortages in Niger are now easing slightly after the first distributions of food aid by international agencies. Action intensified after the country's plight was brought to international attention in mid-July. Where the system is working best, such as in the western town of Ouallam, households are now receiving a monthly food allowance of 100kg of rice. The start of the rainy season should help too.

Nonetheless, thousands of households continue to starve in the provinces of Maradi, Zinder and Tahoua (see map). Recent statistics released by Médecins Sans Frontières, the main NGO in the area, show that 15 children are still dying every week in Maradi. And the geographical difficulties of getting food to the worst affected areas remain. Niger is a landlocked country, and most food aid has to be imported by bad road hundreds of kilometres from the ports of neighbouring Benin, Togo and Nigeria. And then only a few big cities and towns in Niger itself are connected by paved roads; 85% of the people live in remote rural areas.

Even where there is food, it is often too expensive. Though food was imported to compensate for the damage to last year's harvest caused by drought and a catastrophic invasion of locusts, prices rose because of hoarding. Now many nomadic herdsmen and subsistence farmers have lost their animals, and thus the ability to sell their assets to buy food, let alone survive another period of possible drought, should that happen. Others have become too weak to till their plots of land, reducing their chances of surviving beyond this immediate crisis as well.

Food shortages have affected some areas in other countries of the region that were also struck by drought and swarms of locusts. According to a big British NGO, Oxfam, 2.2m people have suffered food shortages in Mali, 700,000 in Mauritania and about 500,000 in Burkina Faso. But most NGOs agree that the immediate problem has now been contained. This may reflect the fact that other governments in the region were quicker to alert international donors to the impending food shortages after the harvest failure than Niger's. Mali has been benefiting from both international food and financial assistance since early in the year.

AP

Indeed, Niger's government has been accused of trying to cover up the extent of the food shortages in order to save face. It was mounting pressure from opposition parties and local NGOs that finally forced the

prime minister, Hama Amadou, as late as the end of May, to acknowledge the “severe food insufficiency” in the country and to ask for international help. It only recently started distributing free food, and has done little to encourage the substitution of failing local crops such as millet, sorghum and beans with other easily accessible crops such as potatoes and yams. These are the longer-term problems that the government needs to address.

Storing up for the future

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Uganda

The limits of freedom

Aug 18th 2005 | KAMPALA
From The Economist print edition

The arrest of a high-profile journalist augurs ill for democracy

ANDREW MWENDA is young, clever, boisterous and a snappy dresser. He is also probably Uganda's best known and most outspoken journalist, with his own show on radio KFM and a column in Kampala's leading private newspaper, the *Daily Monitor*. The fact that he and other independent voices have flourished in Uganda under the long rule of Yoweri Museveni has been taken as proof of the president's democratic values. But on August 12th Mr Mwenda was charged with sedition, a crime which carries a possible five-year prison sentence, and thrown into jail.

He has since been released on bail, but is due back in court later this month. KFM was closed down by the authorities. With an already bitter presidential election due in eight months, even Mr Museveni's biggest fans are wondering why a man committed to democracy would try to bludgeon his media critics into silence.

Mr Mwenda's alleged offences were twofold. In his newspaper column, he wrote that Uganda was planning to attack neighbouring Rwanda. He also used his radio programme to blame the government for the death on July 30th of John Garang, the vice-president of next-door Sudan, who was killed when the Ugandan presidential helicopter he was flying in crashed. Harsh words, perhaps; but they hardly should have earned Mr Mwenda a spell in the clink.

The official broadcasting council said that Mr Mwenda's KFM show was likely to lead to public insecurity or violence, endangering the lives of Ugandans in Sudan. Even crazier were comparisons made by some government officials between KFM and the venomous Rwandan radio station, Mille Collines, that helped incite and orchestrate the 1994 genocide. Mr Museveni has also threatened to close the *Daily Monitor*, in which the Aga Khan has a hefty stake, as well as two other independent newspapers, if they continued to “play around” with security matters.

Such threats are nothing new, say media-watchers in Kampala, Uganda's capital. When the government is under pressure—as over the circumstances surrounding Garang's death—it has often squeezed the press. And that pressure seems unlikely to abate before the presidential election in March 2006. Mr Museveni has already amended the country's 10-year-old constitution to abolish presidential term limits and so allow him to run again. A heated campaign is expected, fought along multi-party lines for the first time since 1980. Observers worry that the harassment of Mr Mwenda and KFM is but a prelude to what may happen next year.

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China

Hu's in charge

Aug 18th 2005
From The Economist print edition

Reuters

China's president is increasingly revealing himself to be an authoritarian. We report how in this article, and in another

Get article background

IN THE nearly three years since Hu Jintao assumed the leadership of the Chinese Communist Party, his image has changed markedly. Mr Hu was once seen by many as a potential liberal reformer—admittedly an assessment drawn from limited evidence. Now, he is widely regarded as a conservative authoritarian. Many Hu-watchers had seized on signs that he might be determined to open up China's secretive bureaucracy. Now, he is said to be holding up Cuba and North Korea as examples of how the party should keep its ideological grip. While Mr Hu has probably changed far less than his mercurial portrayal might suggest, it is increasingly clear that China under his leadership has wavered over economic reform and shunned political liberalisation.

Mr Hu's (in fact, fairly consistent) conservatism has been evident in his belief that the Communist Party, riddled with corruption and other abuses of power, is quite capable of cleaning up its own act without the need for any checks or balances. This year, for instance, he has ordered millions of party officials to take part in many hours of mind-numbing ideological training designed to tighten party discipline (known as the “education campaign to preserve the advanced nature of Communist Party members”).

More seriously, advocates of bolder economic reform have worried about a campaign against “neo-liberal” economic theories that sputtered into life early last year. This apparently stemmed from the worries of party leaders, including Mr Hu, that the cause of free markets and small government could, if given too free a rein, cause an economic meltdown in China similar to that seen in some Latin American countries. On the orders of senior officials, the Chinese Academy of Social Sciences formed a research team and in June last year published a book of essays that proclaimed on its cover that Latin America and the Soviet Union had been “major disaster areas of neo-liberalism”. It said reforms of state-owned industries should be guided by “Marxist theory”.

Publicly, Mr Hu's comments have been moderate in tone. But he has been tougher at closed-door gatherings, such as during a meeting of the party's Central Committee last September. The plenum was of crucial symbolic importance for Mr Hu. It appointed him as the supreme commander of China's armed

forces, thus completing his takeover of the country's three top positions, following his appointment as party leader in November 2002 and president in March 2003. The contents of Mr Hu's maiden speech have not been published in full. In the still secret portion, Mr Hu reportedly railed against “Western hostile forces” and “bourgeois liberalisation”. It was a worrying throwback to the paranoid language that suffused official rhetoric in the wake of the Tiananmen Square protests of 1989.

Yu Jie, a dissident writer in Beijing, says the authorities have stepped up harassment of liberal intellectuals in recent months. Dissidents who have expressed their views online have been particular targets. Mao Yushi, a liberal economist, says public discussion meetings held by his privately run public-policy think-tank, Unirule, have been banned, as have his writings. Unirule has been stripped of its official registration.

Cao Siyuan, another liberal economist who runs a private consultancy, says the attacks on neo-liberalism have coincided with a marked slowdown in the pace of state-owned-enterprise reform. He points to a campaign this year against management buy-outs of such enterprises, a once common form of privatisation in China. The government feared the practice was leading to rampant asset-stripping and was fuelling public resentment. Mr Cao, whose calls for political reform have earned him constant surveillance by the police (he skilfully evaded them to meet your correspondent), says the drawbacks of management buy-outs have been exaggerated by conservatives.

Yet for all Mr Hu's rhetoric, he has yet to strike out at perceived wayward tendencies with anything like the vigour shown by Mao Zedong, Deng Xiaoping or even Jiang Zemin, whose crackdown on Falun Gong, a spiritual movement, in 1999 sent many thousands to labour camps. The complaints of Beijing's intellectuals are offset by other signals that China's economic reforms are continuing, even if government enthusiasm for the kind of mass privatisation of state-owned enterprises that occurred in the late 1990s and early this decade may have abated. In February the government issued new guidelines for private investment in areas hitherto the preserve of the state. This month it issued a draft of China's first law on property rights, aimed at protecting individuals and companies from arbitrary appropriations by the state. Many say the new law is inadequate, but it is still something of a concession to a growing middle class.

Even in the realm of privatisation, the government continues to experiment. In May, a new attempt was launched at off-loading state-owned shares in the 1,400 companies listed in China's stockmarkets. The government has indicated that the reform plan will not mean selling off its controlling stake in “key enterprises”. But it will relinquish at least some of its firms.

Given the increasingly conspicuous inequalities emerging in China as a result of the country's embrace of capitalism, it suits Mr Hu to appear to pour cold water on the idea of laisser-faire economics, blamed for a growing gap between rich and poor, between regions and between urban and rural areas. In the past couple of years there has been an upsurge in the number of protests triggered by these disparities, as well as by rampant corruption. Mr Hu is trying to strengthen the party's legitimacy by stressing its sympathy for the disadvantaged.

Mr Hu's catchphrase is “balanced development”. This will be a central theme in a new five-year economic plan (a still cherished relic of the central-planning era) due to be discussed by the Central Committee in October and ratified by the legislature next March. It will be Mr Hu's first opportunity to put his stamp on a long-term economic strategy. But rapid growth will remain his first priority. Mr Hu has shown no sign of retreat from the core belief of party leaders since the early 1990s: that growth is essential to social stability and thus the party's survival. If redistributing wealth were to jeopardise that, even the conservative Mr Hu would back off.

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China's media

Back on the leash

Aug 18th 2005 | HONG KONG
From The Economist print edition

China appears to regret opening up its media industry

Get article background

OVER the past two years, something remarkable had started to happen in China. Its Communist Party seemed to be tentatively relinquishing its hold over the media—jealously guarded by all totalitarian regimes. Chinese journalists were more aggressively chasing stories and exposing corruption. Foreign media giants were being invited to share their cash and expertise in return for access to China's huge domestic market. And the lure of a foreign stockmarket listing was dangled before big newspaper groups and CCTV, the national broadcaster.

Behind this policy lay an economic imperative: to transform the state media from a loss-making drain on government finances into a globally competitive industry. To attract advertisers and consumers, even Beijing's most hidebound apparatchiks realised the media must be allowed to offer better fare than official propaganda and deathly dull speeches.

Recently, however, China's leadership seems to have developed cold feet, perhaps fearing that a free press will lead to calls for political reform. Another imperative may be the need to present a prosperous, harmonious face to the outside in the run-up to the 2008 Olympics. Either way, stories of widespread poverty, disease, brutality and corruption are becoming unwelcome. The regime is shying away from brute censorship: that would spark an international outcry. Instead, it seems to have opted for a creeping reassertion of media control, targeting certain journalists, publishers and bloggers to scare others into compliance. “China knows the most effective censorship is self-censorship,” says Nicolas Becquelin, at HRIC, a China-focused human-rights group.

The latest example is Ching Cheong, a China-born Hong Kong citizen who reports for Singapore's *Straits Times*. On August 5th Mr Ching was formally charged with spying for Taiwan, though the true reason is likely to be linked to transcripts he had access to of conversations with the late Zhao Ziyang about the Tiananmen crackdown, opposed by the former prime minister. This is the second incarceration of a member of the foreign press since the detention last autumn of Zhao Yan, a *New York Times* researcher. Mr Zhao has not yet been charged, but is being held on suspicion of leaking state secrets abroad. In April, meanwhile, a third reporter, Shi Tao, was sentenced to ten years in prison for leaking details to a foreign website of a ban at his paper on reporting public protests. All these cases highlight the increasingly blurred distinction in China's mind between spying and journalism. Under its Protection of State Secrets law, revealing anything that the government deems a secret can count as spying. And spying can carry the death penalty.

The Chinese government's increasingly hardline stance is encapsulated in Document 16, promulgated this spring. Among other things, this banned the practice of *yidi baodao*, or “reports from non-local places”, with journalists travelling to distant cities where, free of their local minders, they could write harder-hitting stories about corrupt local officials or social unrest. “This was the best hope for China developing an open press,” says Mr Becquelin. In Hong Kong, papers critical of China, like *Apple Daily*, are complaining that advertisers are fleeing because of threats to their mainland businesses. Journalists there are suddenly finding it harder to get visas for travel to the mainland.

The Chinese government has also recently got tougher on internet users. Bloggers are now supposed to register their real names or face huge fines. In June, Microsoft agreed to ban the word “democracy” from parts of its MSN website in China. And the government is arresting those, like Shi Tao, who send “sensitive” information to Chinese foreign-based websites like *Epoch Times* and *Buxun*.

Now the crackdown has been extended to foreign investors. On August 4th, five government ministries and media regulators issued new rules to defend “national cultural security” by forbidding any additional

foreign television channels or other cultural imports. On the same day, limits on production deals between foreign and domestic television and film companies were tightened, dashing the expansion plans of the likes of Viacom, Time Warner and Disney. And on August 17th, China announced a broad crackdown on all media “harmful” to young people.

Reform often proceeds in fits and starts in China. But the comprehensive nature of this about-face on media deregulation points to hardline convictions at the top. President Hu Jintao seems determined to avoid even a hint of *glasnost*, which he is said to blame for the collapse of the Soviet Union. In China, for now, the sword is still mightier than the pen.

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Japan

Honey, I'll shrink the state

Aug 18th 2005 | TOKYO
From The Economist print edition

The DPJ is trying to outdo Junichiro Koizumi on structural reforms

Get article background

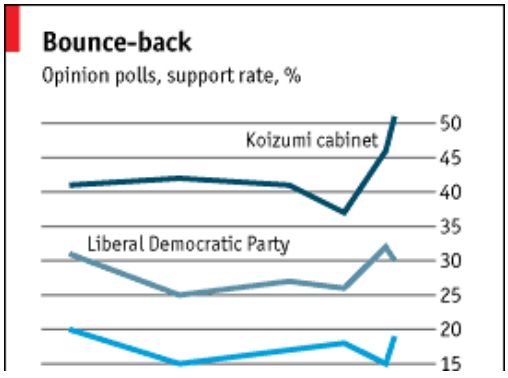
MORE as a sort of public service than anything else, *The Economist* used to devote space every now and then to writing about the Democratic Party of Japan. The DPJ is, after all, Japan's main opposition party. And although the ruling Liberal Democratic Party (LDP) has dominated politics for half a century, the chance that some other party might actually win one day was worth an occasional thought, no matter how often those tentative hopes were dashed. The DPJ does not need charity anymore, however. With the LDP now deeply split over Junichiro Koizumi's failed bid to privatise Japan's postal-savings system, and a cliff-hanger of an election looming on September 11th, the opposition has a real chance to form Japan's next government. The DPJ has thus earned the world's attention. The new question is: what would the party do if it won?

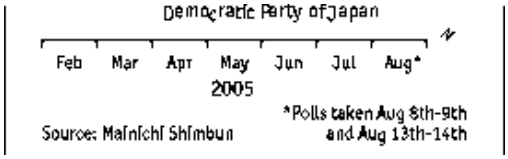
The short answer, which the DPJ has given consistently since Katsuya Okada took over in early 2004, is that it would try to shrink the national government, shake up the bureaucracy, give more power to Japan's regions, and break free of the narrow conservative interests that have long held the country hostage. On all these issues, Mr Okada and his party are trumpeting change even more eagerly than Mr Koizumi, whose passion for budget cuts and "structural reform" has alienated much of his own party. The DPJ has never held power, so it can keep internal divisions on these issues out of the public eye.

Not all of the DPJ's promises involve budget cuts and the economy. The party also criticises Mr Koizumi for angering neighbours. It dislikes, for instance, his annual visits to the Yasukuni Shrine, which makes excuses for the second world war. But it also says that he has cosied up too closely to George Bush. The DPJ pledges to get Japan's (non-combat) troops out of Iraq if it wins. Mr Koizumi countered this week by saying that he does not want Yasukuni to be a campaign issue. Instead of visiting the shrine on August 15th, the 60th anniversary of Japan's surrender, he read out an apology for the war; it followed the lines of the definitive apology offered by the Murayama government a decade ago.

When it released the bulk of its new party platform on August 16th, however, the DPJ made clear that it would stress economic reform during the campaign. There are to be cuts everywhere. Public investment has fallen from 8% of GDP in the 1990s to 5% under Mr Koizumi; but the DPJ wants to slash the central government's public-works spending by another half. It also promises to cut the government's labour costs by 20%. The LDP will feebly try to match this by pledging cuts of 10%.

Overall, the DPJ is promising ¥17 trillion ($155 billion) in gross spending cuts over three years, and ¥10 trillion in net cuts after boosting spending on education, child care and other programmes. It hopes to reduce government borrowing to less than ¥30 trillion a year. The DPJ also backs a rise in sales taxes, which will probably have to be introduced whoever wins.





Since August 8th, when Mr Koizumi decided to fight a snap election over his failed post-office privatisation plan, the prime minister has enjoyed a clear bounce in the opinion polls (see chart). The DPJ, which does not want to appear weak on Mr Koizumi's signature issue (even though, for tactical reasons, it voted against it in parliament that day), has put forth its own rival plan to cut Japan Post's ¥330 trillion of savings and insurance assets by roughly half. It would eventually lower the individual limit on postal savings accounts from ¥10m now to ¥5m, it says.

In a close election, the DPJ might need a partner to govern. That might prove awkward. But, even if it did not, would the economy actually respond to sharp spending cuts? It is doing better these days, but will take time to recover its old vigour. Yet, whatever the economic risks, the DPJ's fiscal samurai, having taken out their cost-cutting sword in the public square, may feel compelled to use it if they win.

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Sri Lanka

The Tigers' prey

Aug 18th 2005 | COLOMBO
From The Economist print edition

The peace process is seriously wounded, but not quite dead

Get article background

AP

A sombre future for Kumaratunga

IT MADE a lousy detective story. There was little chance of proving the chief suspect's guilt; and next to none of bringing him to justice. But the assassination on August 12th of Lakshman Kadirgamar, Sri Lanka's foreign minister, generated tension of a different sort: did it herald the end of the 3½-year ceasefire in the country's 22-year-old civil war? Sri Lanka's president, Chandrika Kumaratunga, seemed to fear so, immediately declaring an indefinite state of emergency.

At worst, the murder might have been a declaration of war by the Liberation Tigers of Tamil Eelam, whose campaign for an independent homeland for the Tamil minority in the north-east of the island has already led to some 65,000 deaths. Just two days earlier, Anton Balasingham, the Tigers' chief negotiator, had given warning of the potential for an explosion of "full-fledged armed confrontation". He was expressing exasperation at the Sri Lankan army's alleged support for a "dirty war of attrition". He accused it of paying and providing logistical assistance to five Tamil paramilitary groups, including one led by a colonel known as Karuna, who split from the Tigers last year. Independent observers think he had a point.

The Tigers had also been angered by the time taken to set up a "joint mechanism" for the distribution in the areas they control of the international aid promised to Sri Lanka after last December's catastrophic tsunami. Agreement on this was eventually reached, though not until June. That led to the withdrawal from the ruling coalition of the Janatha Vimukthi Peramuna, a leftist party that also appeals to ethnic chauvinism among Sri Lanka's Sinhalese majority. Mrs Kumaratunga's People's Alliance has limped on as a minority government, while the joint mechanism has been held up by the Supreme Court's objections.

Having it both ways

Mr Kadirgamar had been a particular target of the Tigers' wrath. A Tamil himself, he was a constant rebuke to the Tigers' claim to be the ethnic group's "sole representative". They saw him as a traitor, who in the late 1990s led a successful campaign in foreign capitals to have the Tigers outlawed as terrorists. By then Tiger assassins had already claimed hundreds of lives, including that of a Sri Lankan president and of a former Indian prime minister.

When the ceasefire was signed, Mr Kadirgamar, who was then in opposition, bitterly criticised its terms. The Tigers, he said in 2003, were a "fascist" organisation, and any cohabitation with them was impossible. Just six weeks ago he had urged Mrs Kumaratunga, and the Norwegian mediators who had negotiated the ceasefire, to demand democratic reform in Tiger-controlled areas.

Yet the Tigers were quick to reject the government's accusations of involvement in Mr Kadirgamar's murder. They blamed the government's own security forces. The Tigers' favoured murder weapon, it was pointed out, is the suicide bomber. Mr Kadirgamar was shot at his home, as he climbed out of the swimming-pool after an evening dip, by a sniper hiding in the house next door.

Perhaps the Tigers hope to have it both ways. Their reign of terror over dissident Tamil voices, which on August 12th had also brought the death of a journalist and her husband, would be strengthened by

evidence that not even their most prominent target was out of their reach. But the denial of responsibility meant there would be no immediate return to all-out war and no withdrawal of the international aid Sri Lanka has been promised.

The initial reaction to Mr Kadirgamar's killing, from both foreign governments and Sri Lanka's, was to appeal for the ceasefire's continuation. In truth, it has long been fraying. The Norwegian-led mission that monitors it has counted 107 political killings in the first half of this year, and some 30 since. It now says the ceasefire is in its most serious crisis yet.

Mr Kadirgamar used to point to evidence that war remains the Tigers' fall-back plan. After the losses they endured in the tsunami, they have stepped up their recruitment of soldiers, including children. They have even acquired a rudimentary air force. Besides the conflict with and among the Tamils, some groups from the Muslim minority, angered at being excluded from the negotiations that led to the joint mechanism, are now reported to be taking up arms.

By removing one of the most powerful and articulate opponents of concessions to the Tigers, and highlighting the dangers of renewed conflict, Mr Kadirgamar's killers may actually have given the ceasefire a short-term boost. But a presidential election is due either this year or next—Supreme Court hearings to decide the date are to begin on August 22nd. With the government in a minority, a general election could also be called at any time. The assassination is likely to boost the electoral chances of those calling for a stronger line against the Tigers.

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Indonesia

From far west to far east

Aug 18th 2005 | BANDA ACEH
From The Economist print edition

A peace agreement in Aceh may serve as a template for Papua

DEFYING the fears of only a few months ago, the Free Aceh Movement (GAM) signed a formal peace deal with the Indonesian government on August 15th, promising to end its 29-year battle for a separate homeland on the northern tip of Sumatra. Both sides have made significant, and unpalatable, concessions. GAM has renounced its claim to outright independence, while the government is giving the rebels a blanket amnesty and is letting people in Aceh province form their own local political parties: something hitherto banned by law in Indonesia, for fear it would encourage the country's fragmentation.

Economic and human-rights provisions have been written into the agreement to ensure that GAM fighters can not only reintegrate into society but can live comfortably and free from fear. That, at any rate, is the theory. Mutual suspicions are so deep-rooted that there is much doubt over whether the disarmament process—whereby GAM is to surrender its weapons and the government in Jakarta is to remove its non-Acehnese military units from the province—will run its planned four-phase course over the next four months. Most people fear that, while regular forces may behave, the numerous proxies both sides have used in the past will be employed to sabotage the deal.

However, signs are that most Acehnese are already reaping the benefits of last month's announcement that an outline deal had been struck. Both sides' troops are, for the most part, remaining in their posts rather than patrolling, so there has been a dramatic decline in violence. Villagers are thus enjoying much greater freedom of movement than at any time since the last, much less structured, attempt at peace collapsed in 2003. Some 250 monitors from the European Union and five South-East Asian nations will help ensure this continues.

While remaining firmly committed to the deal, President Susilo Bambang Yudhoyono has already moved on to the nation's other separatism-racked region, Papua, at the other extremity of the archipelago. In a speech on August 16th to mark Indonesia's independence day, he said he hoped to quell the unrest in the easternmost region, a result of the government's questionable attempts at integration and ham-fisted development efforts, through dialogue and a “persuasive approach”.

Mr Yudhoyono's task will, arguably, be even harder than in Aceh. In contrast to the position of the western province, not all nations recognise Indonesia's sovereignty over Papua (until recently called Irian Jaya), which was confirmed in a stage-managed vote in 1969 by 1,025 hand-picked leaders, rather than in a promised referendum. For the past few years Indonesia's Papua policy has been characterised by big military operations and broken assurances on wide-ranging autonomy. Then again, a few months ago, not many people gave the Aceh peace initiative much chance of success.

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Shipping

Boom and bust at sea

Aug 18th 2005
From The Economist print edition

Landov

How long can the good times last for the shipping industry?

IF TRADE is the lifeblood of the world economy, then the ships that perform the mundane task of transporting goods and raw materials from where they are produced to where they are wanted are the red corpuscles. In 2004, the world's fleets carried around 90% of total global exports worth $8.9 trillion, largely unnoticed. This year, however, shipping firms are attracting the attention of investors as never before. On August 11th Seaspan, a container-ship firm spun out of Canada's Washington Marine, became the biggest of many shipping initial public offerings (IPOs) this year with a $600m listing of its shares on the New York Stock Exchange.

Shipping firms made a total profit of $80 billion last year, an all-time high, according to Martin Stopford, managing director of Clarksons, the world's leading shipbroker. The boom is the result of fast-growing world trade, much of it attributable to China's rapid economic expansion. This has created a vast appetite for raw materials in the country, and ever more manufactured goods to ship back to foreign markets. In 2004 the rate of growth of global trade in goods—many of them carried by sea at some point—was 9%, compared with 5% in 2003 and 3.5% in 2002.

Not surprisingly, such strong demand prompted a sharp rise in shipping rates. Rates for transporting oil in very large crude carriers (VLCCs) hit an average of $86,000 a day in 2004, more than twice their level in 2001-03. The cost of shipping iron ore and coal also hit a peak in 2004. The Baltic Exchange's dry index—covering bulk-cargo rates on the world's 23 busiest sea routes—hit 6,200 in 2004, up from below 900 in 2001. Container shipping and other cargo rates also increased.

Investors have noticed bigger profits, and shipowners have been cashing in with an enthusiasm that suggests they are not entirely convinced that the good times will last. Peter Shaerf of AMA Capital Partners, an investment bank, points out that in 2000 publicly traded tanker firms had a market capitalisation of just $2.5 billion; today the figure is nearer $20 billion. The stockmarket value of firms operating bulk carriers (ships that transport raw materials such as ore, coal and grain) has soared from almost nothing to $5 billion in the same period.

Most of the recent IPOs have involved bulk-carrier operators. Theirs is a highly fragmented business, consisting of perhaps 1,300 firms around the world. Typically, these share offerings are put together by a Greek family-shipping concern, which parcels together some assets and sells a minority stake through companies registered in the Marshall Islands. This small archipelago in the Pacific, equidistant from

Hawaii, Japan and Australia, is much prized among shipowners for its light regulatory touch.

Investors with long memories may feel more than a tinge of concern about some of the people involved in the latest IPOs. Shipping firms that raised cash during the junk-bond mania of the late 1990s were among the worst performers. Bondholders in Enterprisers Ship Holding still smart over a default that cost them $175m. Despite chasing the firm's refrigerated-cargo vessels around the world's ports with court orders and threatening the Restis family with legal action, bondholders have had little recompense. Now the Restis family wants to sell Golden Energy Marine, although its IPO is currently on hold.

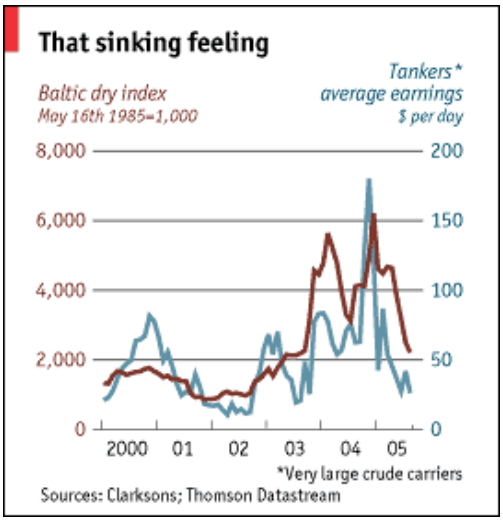
Another Greek shipowner, George Economou, raised $270m with a flotation of DryShips in February. Six years earlier his Alpha Shipping also defaulted on its bonds. Bill Livanos is back a few years after Millenium Seacarriers, his shipping firm, and maritimedirect, a shipping dotcom, went bust. He is planning to raise $114m via a “blank-cheque” IPO—increasingly fashionable on Wall Street—whereby he would sell shares in a shell company with a view to taking advantage of some as yet unspecified future opportunity.

Stormy weather ahead?

The uninspiring track record of some shipowners is but a squall compared with the storms that may be gathering over the horizon. The recent bumper returns from shipping have prompted a ship-building boom. As a result, an armada of new ships is joining the world's fleets just as the rate of growth of world trade may be slowing. According to the Economist Intelligence Unit, a sister company of *The Economist*, the rate of growth of world trade in goods is set to slow, albeit to a still respectable 6.6% this year and 7.0% in 2006.

Might there be a return to the overcapacity that characterised shipping in the 1970s? Mr Stopford points out that last year shipping firms ordered new ships at a cost of $80 billion. The world's shipyards saw their order books expand by one-third in the year to January 2005. They expect to be fully occupied until 2008. In 2000-03 the world's tanker fleet grew by 6m deadweight tonnes (dwt) of capacity. In 2004 alone, it grew by 39m dwt. At the end of 2004 the world cargo fleet, with 889m dwt, was 14% bigger than at the end of 2000, says *Lloyd's Register*. In 2000, orders for new ships equalled only 10% of the fleet's total tonnage. At the start of 2004, 207m dwt of new ships were on order, equivalent to around 23% of the current fleet.

Freight markets are volatile and hard to forecast. Investors in this notoriously cyclical industry may soon be in trouble. In the first half of this year, for instance, rates for VLCCs dropped to half their 2004 level (see chart). Bulk-carrier rates have also plunged in recent months.



Up to 20 more IPOs may take place later this year, assuming that freight rates pick up a little after the summer lull. But most analysts expect rates to slide again next year. According to Drewry, a shipping consultancy, demand is likely to outstrip fleet growth for container shipping this year but could slip behind in 2006, when fleets are expected to grow by a heady 14%.

Yet Seaspan's IPO suggests that some investors still have faith, at least in container shipping, where rates have not (yet) plunged. For tankers and bulk carriers the omens look less good. In July, Genco, a Greek bulk-shipping firm, had to cut the price of its IPO—by some 10%—and it was not the first shipping firm to do so this year.

Mr Stopford says that shipping is not in a bubble but a “super-cycle”. By the 1990s, he says, the industry had finally shed the crushing burden of the huge oversupply there had been since the 1970s and it is unlikely to recreate it. Less optimistic observers suggest that what some now dismiss as a blip is the start of a serious slump.

China's astonishing rate of growth cannot last forever. Indeed, spot rates for bulk carriers in Asia recently hit a two-year low after falling by half from a peak in March as Chinese demand has cooled a bit. And the more slowly growing trade across the Atlantic is vulnerable to any slackening of economic activity in Europe or America. If growth and trade stumble while shipping lines are piling on extra

capacity, the result could be empty holds, plunging shipping rates and rapidly sinking profits.

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British Airways

Catering for suppliers' strikes

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From The Economist print edition

The dangers of outsourcing

BRITISH AIRWAYS paralysed by a strike? It must be August again. In the summer of 2003, check-in staff struck over work changes. Last August came a strike over pay. This year's dispute started last week with a quarrel over the sacking of some 670 staff by Gate Gourmet, BA's inflight caterers. That triggered a one-day (illegal) sympathy strike by 1,000 BA ground staff, again causing chaos for passengers, some 70,000 of whom were stranded. BA's outgoing boss, Sir Rod Eddington, is livid at the latter “outrageous” action by the Transport & General Workers' Union (T&G), which, although officially against the illegal strike, is keen to flex its muscles as BA prepares new working practices for when it moves to Heathrow's new fifth terminal (see article). The catering dispute may be a taste of what is to come, then. It is also a reminder of the dangers of outsourcing.

Gate Gourmet used to belong to BA, so many staff feel it is still part of our family, say T&G officials. Now it is owned by Texas Pacific, a private-equity firm, which bought it from Swissair after that airline went bust in 2001. The T&G objected to the firing of Gate Gourmet workers who had protested against it hiring temporary staff even as it cut 200 permanent jobs.

Union leaders claim that Gate Gourmet had undermined a sensible rescue package that they had agreed in June to cut costs by some £14m ($25m). Texas Pacific says that Heathrow is by far the worst of Gate Gourmet's businesses in 29 countries, losing £23m last year. Archaic working practices, which it says the union refused to change sufficiently, are a big problem.

Hoping to pin the blame on its caterer, BA says that it tried to help Gate Gourmet, offering a deal in July to “improve and extend” their relationship at better rates. BA claims its offer, coupled with a deal with the T&G, would have secured the future of the firm. But, says Texas Pacific, some of the terms of the agreement were “inimical” to Gate Gourmet, such as exposing the caterer to more risk by guaranteeing its Heathrow contract only for a year.

The strikes are a financial and, worse, a reputational blow to BA. There will be immediate revenue losses, estimated at £40m-60m, plus longer-term losses from passengers who stop flying with such a strike-ridden airline. Given the critical importance to its brand of maintaining service, BA should have prepared a contingency plan to protect itself against a strike, says Yossi Sheffi, a logistics expert at MIT and author of a forthcoming book, “The Resilient Enterprise” (MIT Press). BA should either have used more than one caterer, he says, or else had such a close relationship with Gate Gourmet's managers that it knew exactly what they were up to.

BA is thus having to learn the same truth about outsourcing that has already been discovered by firms ranging from banks criticised for poor customer support from outsourced Indian call centres to Nike and Gap, attacked over the sweatshops allegedly operated by some of their suppliers. Outsourcing an activity does not mean it is no longer a firm's problem.

Meanwhile, Gate Gourmet may go into administration, where restructuring will be easier—if BA does not first kill the firm by finding a new caterer. But only the market leader, LSG Sky Chefs (part of Lufthansa), is big enough to prepare the 80,000 meals a day BA needs. So it is in the ideal position to demand a higher price.

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Media firms

Icahn's latest prey

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Time Warner would be wise to take Carl Icahn seriously

TIME WARNER should sweat a bit more, thinks Carl Icahn, a veteran corporate raider and activist shareholder. He sniffs at the media firm's plan to float a 16% stake in its cable business next year, and to buy back $5 billion-worth of its own shares. Instead it should spin off the cable business and spend $20 billion buying back its own shares if it wants to put some serious zip into its share price, he said this week.

Mr Icahn, aged 69, has a long record of biffing firms on the nose, and sometimes getting biffed in return. In the 1980s he fought lucrative proxy and courtroom battles with Texaco, Phillips Petroleum, TWA and US Steel. Then he was seen as a dangerous maverick. Now his methods are the model for legions of hedge funds that buy stakes in firms with the aim of interfering.

As often before, Mr Icahn is aiming high. Time Warner is the world's biggest media group, with a market value of about $81 billion, and Mr Icahn speaks for only about 2.6% of its shares, held by a hedge fund he controls and three more funds which have teamed up with him.

But he is tapping into a general impatience with media firms on Wall Street, and a restlessness within the firms themselves about their underperformance since the 2000 internet bust. Viacom is breaking itself in two (though even that is not doing much for its shares). News Corporation has announced a share buy-back plan. Shares in Dow Jones, publisher of the *Wall Street Journal*, leapt briefly this week amid rumours that some members of the controlling family might want to sell.

Time Warner has been recovering steadily from its disastrous surrender to America Online (AOL), an internet operator that bought it with wildly overvalued paper in January 2000, just before the bubble burst. The old Time Warner businesses— film, publishing, broadcasting, cable-television—have regained the upper hand over AOL. But small wonder if the memories of that turmoil have left the group risk-averse and wary of borrowing or spending too much. Net debt at the end of 2004 was equal to barely one-quarter of the group's $61 billion equity.

Time Warner's main passion now is for its cable business, America's second biggest, which delivered almost 30% of the group's $6.2 billion operating profit last year. This year Time Warner joined with Comcast, the industry leader, to pay $18 billion for Adelphia Communications, a troubled rival, and to share its subscribers.

“We like this business, we've said it a gazillion times,” Time Warner's boss, Richard Parsons, told analysts recently. Others fear that the Adelphia deal will tie up Time Warner's capital without creating economies of scale. Mr Icahn seemingly thinks that the market would value the cable business, and the rest of Time Warner, more highly as separate entities than as combined ones, or perhaps that a spun-off cable business would tempt a private-equity or a trade buyer at a fancy price.

Jessica Reif Cohen, an analyst at Merrill Lynch, thinks that Time Warner could easily afford to raise its share buy-back target to $10 billion, and that even $20 billion would not be an “unreasonable” stretch. That leaves the cable spin-off, a more difficult demand requiring Time Warner's management to reverse itself.

If the fight gets rough, Mr Icahn will no doubt find more allies and lines of attack. Anthony Noto, an analyst at Goldman Sachs, said earlier this month that Time Warner would do better broken up, but proposed AOL as the division to go first. By August 17th, Time Warner's shares had risen by 8% since rumours of Mr Icahn's interest began to spread at the start of the month, enough to net his investor group a paper profit of about $160m. Whatever follows for the brands and profits of Time Warner, the brand and profits of Carl Icahn have done very nicely already.

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Undergraduate recruitment

In search of the ideal employer

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Students are in demand again and becoming increasingly choosy

COME September, the campuses of America will be swarming not just with returning undergraduates, but also with employers set on signing up the most able 10% of them. “We are seeing a far more competitive market for talent,” says Steve Canale, a recruitment manager at General Electric (GE). Students who recently could have expected two or three offers in their final year are now getting as many as five. To gain a competitive edge, firms are arriving ever earlier on campus with their recruitment caravans. They are also starting to look at (and select) summer interns more as potential full-time employees than as mere seasonal extra hands: 60% of GE's graduate recruits in America this year, for instance, will come from its crop of more than 2,000 interns. Many interns will have employment contracts in their pockets before they even return for their final year of study.

Firms are working harder to polish their image in the eyes of undergraduates. Some have staff who do little but tour campuses throughout the year, keeping the firm's name in front of both faculty and students, and promoting their “employer brand”. GE focuses on 38 universities where it actively promotes itself as an employer. PricewaterhouseCoopers (PWC), an accounting firm, targets 200 universities and gives a partner responsibility for each. PWC says that each of these partners spends up to 200 hours a year “building relationships on campus”.

That particular investment seems to have paid off. Each year Universum, an employer-branding consultant, asks some 30,000 American students to name their ideal employer. In this year's survey, published recently, PWC came second (up from 4th in 2004), topped only by BMW (see table). Yet the German carmaker, which knocked Microsoft off the top spot, steers clear of campuses, relying for its popularity, says Universum, on the “coolness” of its products.

The good workplace guide
American undergraduates' ideal employers

Company	2005	2004
BMW	1	2
PricewaterhouseCoopers	2	4
Ernst & Young	3	6
Boeing	4	7
Johnson & Johnson	5	17
Deloitte	6	8
Coca-Cola	7	5
Microsoft	8	1
CIA	9	14
FBI	10	138
Merrill Lynch	11	12
IBM	12	11
Apple Computer	13	41
KPMG	14	16
J.P. Morgan Chase	15	18

Source: Universum Communications

Students, it seems, are heavily influenced in their choice of ideal employer by their perception of that employer's products and services. Soaring up this year's list were Apple Computer (from 41st to 13th) and the Federal Bureau of Investigation (from 138th to 10th). The success of Apple's cool iPod has had a powerful effect on the firm's ability to recruit top undergraduates. Likewise, the positive portrayal of the FBI in some recent films and TV shows has allegedly helped with recruitment.

The accounting firms say that the fall of Enron and Arthur Andersen has done their recruitment no harm: instead, they claim, it has made students realise that accounting is not mere number-crunching, but also involves moral judgments. The “Big Four” accounting firms are all among this year's top 15 ideal employers.

Undergraduates now do much of their research into future employment online. There seems to be a close correlation between their choice of ideal employer and their choice of most impressive website—where PWC, Microsoft and Ernst & Young win gold, silver and bronze respectively.

Even so, some top firms think they still appreciate the personal touch, and are sending their most senior executives to campuses to meet students and to give speeches. “The top attracts the top,” says Claudia Tattanelli, boss of Universum in America. Jeffrey Immelt, GE's chief executive, is a keen on-campus speaker and has visited six leading universities in the past year. In the process, he may have shaken

hands with one of his successors.

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Khazanah

The Malay way of business change

Aug 18th 2005 | KUALA LUMPUR
From The Economist print edition

An attempt to revive Malaysia's underperforming state-owned firms

"YOU either execute or get executed," says Azman Mokhtar, of his mission to overhaul Malaysia's 40-odd partially state-owned firms. Last year, his appointment as head of Khazanah, the government's previously passive holding company, caused the publicly traded shares of various "government-linked companies" (GLCs) to soar. Briefly, the shares of Telekom Malaysia, the biggest firm in Khazanah's portfolio, were up by over 50%. But the shine is beginning to wear off, as investors start to realise how tough his job is.

The GLCs make up only 5% of the firms listed on Malaysia's stockmarket, but account for 36% of its market capitalisation. Yet on every measure but size, Mr Azman points out, they have underperformed. One study found them to be more highly indebted than average, to generate less profit per worker and to earn a lower return on equity. In the five years before he took over, shareholders made a total return of 3.6% on GLCs, and 7.5% on other firms in Malaysia's stockmarket index.

The biggest firms in the Khazanah stable have bureaucratic origins: they are either former monopolists, such as Tenaga Nasional, a power firm, or pet government projects, such as Proton, a carmaker. Political considerations often trump commercial ones. All GLCs, for example, favour ethnic Malays when dispensing jobs or contracts, in line with the government's policy to get more Malays involved in business. Politicians often seem to end up in cushy jobs as advisers or board members.

Mr Azman's solution is a strong dose of corporate discipline. He has appointed young, foreign-educated professionals to run Tenaga and Telekom. Senior executives are now on fixed-term contracts, with extensions and pay linked to performance. Government officials with a regulatory role have been booted off boards. Suppliers (even the Malay ones) now have to bid for contracts, rather than stitch them up in backroom deals. This new policy, Mr Azman says, cut the cost of one transaction from 100m ringgit ($27m) to 12m.

Nationalism is also out of fashion. Last year, Khazanah sold a 5% stake in Telekom to Temasek, its Singaporean counterpart. Temasek's previous attempts to buy shares in Malaysian GLCs had been rudely rebuffed. An American now runs SilTerra, Khazanah's struggling microchip foundry; a Dutchman runs Rapid KL, which operates commuter trains in Kuala Lumpur.

Such reforms are also being adopted by the government's other investment agencies, such as the state pension fund and a government-backed fund for Malays. Last month, the agencies jointly launched a "Transformation Manual", with prescriptions for everything from revamping boards to cutting procurement costs.

But the government is still shying away from other reforms. Big layoffs are taboo. Instead, Telekom has had to launch a voluntary redundancy scheme to shed one-tenth of its staff. Tenaga is now squeezed between costly power-purchasing contracts foisted on it by the previous government and low tariffs insisted on by the current one. And Mahathir Mohamad, a former prime minister who created Proton to be a national icon and now advises the firm, is resisting selling a controlling stake in the firm to a foreign carmaker.

At those GLCs that are still obliged to do charitable works on the government's behalf, Mr Azman is pushing for a clearer definition and delimitation of their responsibilities. Before taking over Khazanah, for example, he masterminded a restructuring of Malaysian Airlines, whereby the government agreed to absorb the losses on the carrier's unprofitable domestic routes.

In short, Khazanah is not seeking to end the government's meddling, but to rationalise it. Mr Azman still argues against selling poorly performing hi-tech firms, such as SilTerra, lest that deprive Malaysia of the

associated industry and technology transfers and the jobs that come with them. Future generations, he says, might curse him for such a move. On the other hand, if he runs up a big bill for taxpayers, future generations might curse him even more for keeping SilTerra afloat.

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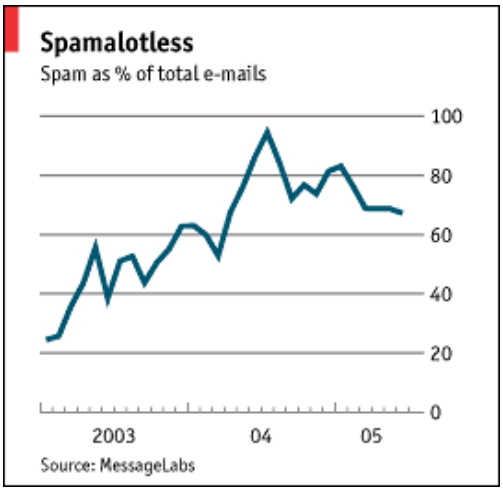
Internet security

Winning the war on spam

Aug 18th 2005
From The Economist print edition

Unwanted e-mails are no longer the menace they once were

IT IS the scourge of e-mail inboxes, plying cheap drugs, septic tanks, new mortgages and bigger manhoods. But “spam”, unsolicited e-mail, seems to be in retreat. The amount of spam that swishes through the internet is holding steady or declining, according to most studies. And of the stuff that still exists, the vast majority is blocked by filters before it gets to an inbox.



Just a few years ago, newspapers ran scary headlines saying that spam would swamp the internet. Legislatures scrambled to enact laws. Tech firms were handed fortunes by venture capitalists to eradicate it. Today, though still plentiful, spam is hardly the menace it once was. According to MessageLabs, an e-mail services firm, spam decreased from 83% to 67% of all e-mails sent between January and June.

Several factors explain spam's decline. Filtering technology, provided by firms such as Postini and IronPort, has become so effective that it blocks around 95% of spam. And users have become wiser to spam scams, and many now ignore them. This has undermined the business model of spam, prompting spammers to move on to more targeted and lucrative online attacks. In particular, “phishing”—fraudulent e-mails that try to trick users into divulging financial information by posing as well-known banks or websites such as eBay—has grown enormously in the past year.

The law has also played a part. On August 10th, America Online, an internet firm, won a $13m judgment under the CAN-SPAM Act of 2003, which lets firms seize spammers' assets. One spammer, who co-operated in the investigation, agreed to surrender not just $75,000 in cash and $20,000 in gold bars, but also his yellow 2003 Hummer H2 (which formerly bore the licence plate “CASHOLA”). A day earlier, Microsoft settled a lawsuit with Scott Richter, the so-called “Spam King”. Mr Richter paid the firm $7m, and agreed to comply with anti-spam laws and have his marketing firm monitored for three years by New York's attorney-general.

In the past two years, Microsoft has filed over 100 lawsuits against spammers in America, and sued or supported legal action by governments in 30 cases in other countries. So far, it has won or favourably settled half of the cases (and lost only one, early on). In around two-thirds of cases, Microsoft relies on old consumer-protection and fraud laws rather than new legislation specifically designed to counter spam (though the firm supports spam laws, as they tend to eliminate legal loopholes). “I think they have a deterrent effect,” says Brad Smith, Microsoft's general counsel, “though nothing is a panacea.”

For spammers who get caught—admittedly a tiny minority—the consequences can be severe, far beyond the loss of a Hummer. For instance, in April, a Virginia judge sentenced a spammer to nine years in prison, though the sentence has been suspended pending an appeal. In December 2004, a federal judge in Iowa ordered two spam firms to pay over $1 billion to a small internet service provider, after its e-mail system got clogged (it is unlikely the firm will collect any money).

Even so, spam remains a serious burden. The costs it imposes include $3 billion a year spent on anti-spam technology in America and lost output that some estimates put at $50 billion worldwide. A study in 2003 by the Pew Internet & American Life Project found that over half of all internet users said that spam made them less trusting of e-mail, and one-quarter said it led them to reduce their use of e-mail. A report in June by Gartner, a research firm, forecast that consumer unease—due to spam and other online threats such as phishing, viruses and worms—will slow e-commerce growth in America by

up to 3% in the next three years. (This week two worms, Zotob and Rbot, caused problems at some big American media firms.)

But spam, at least, is in decline, which ought to be cause for celebration, particularly since it once seemed so unstoppable. In January 2004, at the World Economic Forum in Davos, Switzerland, Bill Gates of Microsoft brashly predicted: “Two years from now, spam will be solved.” At the time, technology pundits snickered. Mr Gates suggested that new techniques to identify senders, or the imposition of a small fee to send e-mails, might solve the problem. Mr Gates was wrong, in that those approaches were not adopted and spam remains pervasive. And yet, paradoxically, his optimism was justified.

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Wireless broadband

Why wait for WiMax?

Aug 18th 2005
From The Economist print edition

Wireless broadband access is taking off, even before WiMax arrives

WHAT has become of WiMax? This is the wireless technology that is supposed to be about to take over the world, by extending Wi-Fi-like broadband internet access, now available only in small “hotspots”, to whole cities, or even whole countries. But, like most new wireless technologies, WiMax is late: testing to make sure gear from different vendors works together is taking longer than expected, and the first WiMax products will not be available until early next year. Even then, WiMax seems unlikely to live up to the initial hype from its proponents, foremost among them Intel. A recent report by Forrester, a consultancy, called for a “reality check” and predicted that the real impact of WiMax will not be felt before 2010.

But while WiMax is still stuck on the starting blocks, rival technologies that do the same sort of thing, but are available now, are taking off. In the past few weeks, T-Mobile has announced that it will build a nationwide wireless broadband network in the Czech Republic, using technology provided by IPWireless. The same technology, already deployed in parts of Germany, Britain and New Zealand, will also be used by Netcom Africa to provide wireless broadband access in Nigeria.

Meanwhile, a rival technology from Flarion will be used to provide wireless broadband coverage across Finland, initially in rural areas where fixed-line broadband connections are currently unavailable. On August 11th, Qualcomm, the company that pioneered the technology that underpins third-generation (3G) mobile phones, announced that it would buy Flarion for around $600m, chiefly to gain access to its intellectual property, which is widely expected to form the basis of post-3G networks.

Both IPWireless and Flarion technologies combine fast, Wi-Fi-like internet access with the wide-area “works anywhere” coverage of mobile phones. Slot a suitable card into your laptop and you have a broadband connection you can carry around. Hitherto, such technologies have been used in a few regional networks and small-scale trials. Now they have made the crucial breakthrough to deployment in large-scale, national networks.

Paradoxically, one big factor that has spurred interest from operators is WiMax hype. “WiMax has opened up a lot of operators' eyes,” says Ronny Haraldsvik of Flarion. But they then realise, he says, that WiMax is not yet available, and even when it is, it will initially only support access from fixed locations. The first WiMax devices will be boxes to be fixed to the outside of homes or offices to provide broadband access, and cannot be moved; mobile WiMax is still years away. As well as being mobile, Flarion and IPWireless “are technologies that work today,” says Mike Thelander of Signals Research, a consultancy.

Another factor, says Chris Gilbert, boss of IPWireless, is disappointment with 3G phone networks, which have now been launched in western Europe after much delay. These were expected to provide broadband access over wide areas, but have failed to deliver the high speeds once promised. Operators in eastern Europe, which have yet to build 3G networks, can see that 3G is not the gold mine originally predicted, and are considering alternatives. Roland Mahler, boss of T-Mobile's Czech division, says there was insufficient demand to justify the expense of a 3G network, whereas the IPWireless technology can be marketed as an alternative to fixed broadband, for which demand is clear.

Does this mean that WiMax will be squeezed out by the other technologies it has unwittingly boosted? In fact, it looks as though there is room for a mix of technologies, each with its own strengths, depending on the availability of spectrum, the regulatory regime, and the needs of various types of operators. In several countries, including the Czech Republic, Romania, Nigeria and Argentina, a wireless-broadband technology called CDMA450, which is ideal for rural coverage, is being deployed. In western Europe, mobile operators that are committed to 3G are likely to upgrade to an improved version of it called HSDPA, which will offer higher download speeds, comparable to those of fixed-line broadband.

WiMax, which can be used in unlicensed (and therefore free) spectrum, will particularly appeal to “non traditional” operators such as regional start-ups, but will be just “one among many” technologies, says Mr Thelander. It will also be used by fixed-line operators, which do not require mobility, to plug gaps in their fixed-line broadband coverage, for example in remote and rural areas.

In places with little or no fixed-line broadband, wireless alternatives have obvious appeal. And where fixed-line broadband is available, wireless technologies will offer the bonus of mobility—the ability to take your broadband connection with you. The flavour of technology is not terribly important. What matters is that broadband, like telephony, no longer requires wires—which will help to increase access in rural areas and in the developing world. Let a thousand networks bloom.

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Face value

Trying a new pitch

Aug 18th 2005
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JWT

Bob Jeffrey is trying to rebrand a grand-daddy of advertising

"AS PIONEERS of advertising it is time for us to trail blaze again," announces the corporate website of JWT. By changing its name earlier this year to a more fashionable abbreviation, the advertising agency formerly known as J. Walter Thompson has resorted to the oldest trick in the book for its own rebranding. This change is supposed to mark a rite of passage: away from a media market dominated by 30-second commercials on mainstream TV channels toward one in which clients chase consumers along multiple routes across an increasingly fragmented media landscape in which the internet is crucial.

Changing the name of America's biggest, and the world's fourth-biggest, advertising agency was a symbolic but necessary measure, insists Bob Jeffrey, who became JWT's global head in January 2004. Anyway, he adds, many people were already referring to the agency by its initials. But it will need more than symbolic changes for this giant, or its rivals on Madison Avenue, the spiritual home of America's advertising industry, to survive and prosper in the marketing future now unfolding.

The good news is that after a deep slump, advertising spending is growing again. The global ad market could be some 4.7% bigger this year than last, with spending of over $400 billion, forecasts ZenithOptimedia, a research company. However, less happily, Zenith says that growth in spending on TV commercials has already peaked, and may begin to shrink—just as spending on advertising is already shrinking in other traditional media, such as newspapers and magazines. The fastest growing part of the advertising market is now the internet, accounting for more than 5% of America's total ad spending last year. Internet advertising is forecast to double in value within a few years.

"There is not one CEO that I have talked to that hasn't got the message about how rapidly communications are changing, and the influence of technology," says Mr Jeffrey. But simply rushing to plaster websites with irritating ads that get in the way of what users are trying to do is hardly the way forward, he acknowledges. Many people in developed markets consider themselves "time poor". And that, argues Mr Jeffrey, means that consumers are increasingly likely to resist marketing methods that demand significant amounts of their time and attention.

JWT seems to have the strengths needed to confront these changes: a glorious 141-year history, a worldwide staff of 8,500 and a list of blue-chip clients including Ford, Unilever and Pfizer. But will any of these really be strengths? In the future many traditional elements of its craft may no longer work. So Mr

Jeffrey is launching what he claims is a revolution. “We are basically changing everybody's roles and responsibilities.”

Advertising has traditionally been run in a sort of linear way: an agency would find out what consumers thought about a client's product, use that as the basis to develop a campaign to promote the product, and then monitor and evolve the campaign as it proceeded. Now the process has to become more “holistic” and account managers need to be “executive producers of ideas”, says Mr Jeffrey. Creative ideas can emerge from all sorts of places and be used in many different ways to engage consumers and persuade them “to spend time with the brand”, he adds. Television can still be part of the process—after all, lots of people still watch it—but it is no longer at the centre.

The coming launch in America this autumn of a new Ford Fusion car provides an example of where advertising is going. Even before the car has gone on sale, the campaign has begun with the creation of a website. Among other things, the website promises a series of “flash concerts” by some leading rock bands and hip-hop artists. These are musical events to be held at secret locations and announced at the last minute via e-mail and text-messaging. Ford—through JWT—is doing this because it hopes to win more younger, urban buyers for its car.

Partly in anticipation of this more complicated market, many ad agencies have clustered into four big global groups that bring together a wide range of resources, from public relations to direct marketing and media buying. They are America's Omnicom and Interpublic, France's Publicis and Britain's WPP, of which JWT is a part. In a significant recent development, some big accounts are now being won by an entire group, rather than by individual agencies. WPP, for instance, has won global responsibility for the accounts of HSBC and Samsung. But how strong a trend this will be is unclear, as some big advertisers still say they prefer to deal directly with individual agencies.

One of the latest accounts to come up for review is that of British Airways, which is finding that the internet is now one of the most important ways to stay in touch with customers and to receive bookings. For over two decades the airline's advertising account, now worth £60m ($108m) a year, has been handled by Maurice and Charles Saatchi, who are sure to fight hard as others bid for it. JWT, along with the Saatchis' agency, is on a shortlist of four agencies that will pitch for the account in September.

How to get ahead in advertising

JWT was the first agency to develop artwork and copy for its clients, so there is something to its pioneering boasts. Can it shake things up again? The firm's ability to be creative will be more crucial than ever, says Mr Jeffrey—which may not be surprising, given that he has held a number of creative posts with other agencies and built his own company before joining JWT in 1998 to run its flagship New York office. He turned that office around en route to becoming chief executive last year. Today, he says, the advertiser should start with an idea and then find the people with the talents, capabilities and resources to carry it out. But those ideas had better be good. Today's consumers not only have more choice than ever, both in terms of goods and media, but also seem less tolerant than ever of the boring or irrelevant.

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Germany's economy

Ready to motor?

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From The Economist print edition

There are encouraging signs that Germany's economy is set to grow more strongly

THERE has been much pessimism about Germany's economy in recent years: too much, perhaps, judging by recent evidence that it has quietly started to do better than most people expected. Among the positive signs has been a strong performance by its big companies, which have reported healthy profits. Even unemployment, for long a black spot, is beginning to fall. And although many Germans still question the case for further economic reform, they have to admit that their country is doing much better than, say, France or Italy, partly because of recent reforms. Suddenly Germany looks relatively healthy, and there are grounds for cautious optimism that things could get better still—but only if the political winds blow in the direction of more reforms. This is why German's general election campaign, which leads to a parliamentary election scheduled for September 18th, could be decisive economically as well as politically.

Unfortunately Germany's reform programme, known as Agenda 2010, became bogged down after meeting fierce opposition soon after its launch in 2003. Since May 22nd, when the election was called, there has been near paralysis. But there have been some positive results from Agenda 2010. These have raised hopes that fresh impetus could set the economy on to its strongest track for years.

The most radical measure has been Hartz IV, a restructuring of unemployment benefit and social security. From January this year things became less cushy for the 1.8m long-term unemployed, who comprise a staggering 38% of the total jobless. Continued benefits are now means-tested, and unwillingness to accept job offers is penalised. Hartz IV has not been an unqualified success. It has added €8 billion ($9.8 billion) to this year's government costs, but failed to create many new jobs. It has, however, made employees more fearful of the consequences of losing their jobs. That has strengthened the hand of firms negotiating new wage deals, and weakened the power of trade unions.

And yet this fillip for the corporate sector has, arguably, been less good for the economy as a whole. In Germany there is a close relationship between fear of unemployment and consumer confidence. In recent years low consumer confidence has held back domestic demand—Germans have been saving more and holding off spending. That has become the single biggest drag on growth.

It was partly the issue of creating new jobs that precipitated the call for new elections. Government and opposition could not agree on the lowering of corporate tax from 25% to 19%, a controversial measure that required their joint agreement.

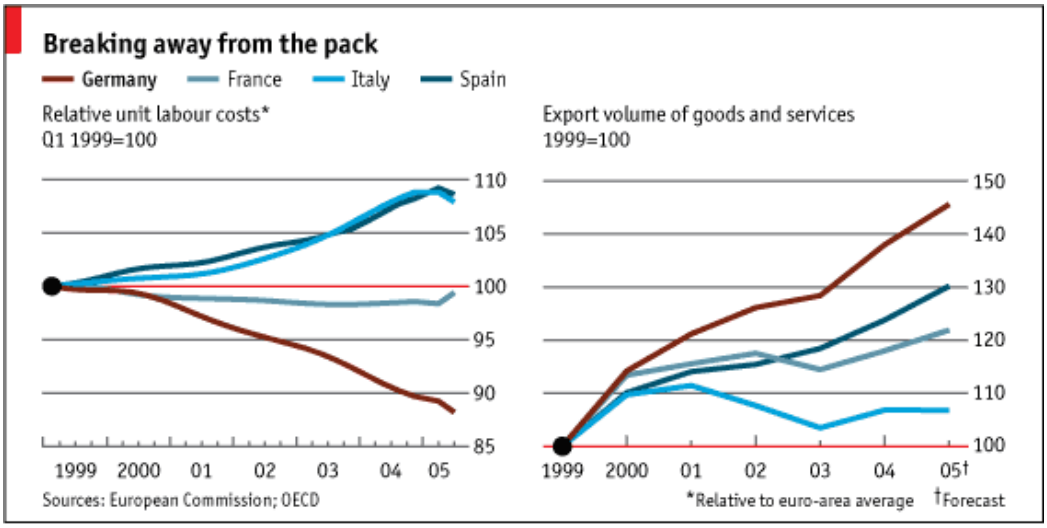
Why have Germans been so lukewarm over far-reaching economic reforms? Otto Graf Lambsdorff, a former economics minister from the liberal Free Democratic Party, blames what he calls

"snuggle-capitalism". Germans, he said in a recent interview, would rather have certainty and equality than freedom. Instead of getting on their bikes to look for work, or setting up on their own, they have a tendency to cling to what they know, consoling themselves that they are all in the same boat.

Change has been happening, however, albeit slowly. The number of self-employed has risen from 4m four years ago to 4.4m at the end of June. So-called "one-euro" jobs, which dignify unemployed people by paying them one euro an hour plus their benefits, have proved popular, with over 200,000 being created, as have "mini-jobs" paying €400 a month, although it seems that these have mostly been snapped up by students and full-time workers wanting to work less, rather than by the long-term unemployed.

One plank of Agenda 2010 was a pact between business and government to create more jobs and trainee positions. In reality it had little impact. The "capital for jobs" scheme was shelved in March 2004 as unworkable. Many firms have failed to deliver their quota of trainee posts, while others that did found the posts were not filled anyway.

Yet the corporate sector offers a striking example of Germany's broader positive economic trends. German companies have shown a remarkable improvement in their competitiveness thanks to a relative fall in their unit labour costs (see chart). Big companies have learned that their main battle is now a global, not a domestic, one. Their profits stem largely from exports to countries where demand is thriving. Indeed, the profits and activities of leading German companies have become somewhat dislocated from the economic fortunes of Germany as a whole.



That trend was hastened in 2003 with a new tax law which allowed firms to sell their cross-shareholdings in other German companies without paying capital-gains tax. This prompted a wholesale unbundling of what had become known as "Deutschland AG". Companies could concentrate on their core business. Their ownership became more international and more demanding of shareholder value.

That has led to huge tensions between the way big companies such as Volkswagen, DaimlerChrysler and Siemens are perceived at home and their efforts to survive as global players. At home they have to deal with a highly unionised workforce and a supervisory board heavily influenced by employee and union representatives, while internationally they must compete with companies whose labour costs are as much as 80% lower. West German workers cost on average €27.60 ($34) an hour, including €12.20 of ancillary costs—the highest in the euro zone—compared with €19.90 an hour in Britain and €18.80 in America. (In east Germany the average is a more modest €17.20.) But in central Europe labour costs are well below €5 an hour.

Surprisingly flexible

German efficiency and once-matchless engineering can reduce that differential and justify higher prices, but only to a degree. Last year and this, most of these companies had reached a point at which only a reduction in their labour costs would support continued production on their home soil. Yet Siemens, DaimlerChrysler, VW and many others managed to cut deals with their workforces, lengthening working

hours and limiting perks, while to some extent guaranteeing employment for the next few years. IG Metall, once Germany's most powerful trade union, had little choice but to go along. Recent research by Morgan Stanley, an investment bank, found that more than 30% of Germany's workforce are now employed in part-time or temporary jobs, meaning that firms can deploy their labour much more flexibly than in the past.

Collective wage-bargaining is not dead—even Germany's conservative political parties hesitate to campaign for its removal. But unions have been pragmatic behind the scenes in order to save jobs. The contrast with, say, France is stark.

For the majority of German workers, companies' growing willingness to shift production to wherever labour and capital costs are cheapest is a direct threat to their jobs. Changing the mindset of a population to think globally rather than locally is likely to be the work of a generation rather than a year or two. But leading companies are growing more assertive about their economic role at home. Continental, a tyre-maker, and one of the best-performing companies in Germany, has located much of its production abroad. But it still employs 32,000 people in Germany and keeps its headquarters there. In the age of globalisation, national champions are national only in the sense that they must have their headquarters somewhere. If it is to keep a quota of champions, then Germany will have to make it attractive for them to stay, and for others to come.

An important measure of progress is that business leaders are beginning to feel more confident. Last month a much-watched index of business confidence rose by more than analysts had expected, perhaps because of the strong profits performance that was evident when the latest set of quarterly results were announced. Two-thirds of Germany's top 30 listed companies produced improved results for the second quarter of the year. That includes jumps of more than 20% over the same period last year by chemicals firms Altana, BASF and Bayer and respectable earnings from energy producers, insurance companies and banks.

Perhaps most important for the health of the economy is the improved position of the banks. All the biggest banks now have their costs and their balance sheets under control. Much of the banks' real-estate portfolios and their non-performing loans secured against property have been sold off at distressed prices. The challenge now is for the banks to take more risk in their lending to medium-size companies. Good performance from them will be needed to underpin a sustained recovery.

The accumulation of positive economic developments includes evidence that the labour market has stabilised. In July unemployment fell for the fourth month in a row. There are 50% more job vacancies than there were a year ago, and surveys suggest that employers are becoming more bullish, expecting to hire more workers in the coming months. Manpower, a recruitment consultant that tracks employers' intentions across the world's big economies, notes that the rise in Germany's indicator has been stronger than movements anywhere else.

Learning to innovate

There are also signs that efforts to improve Germany's long-term economic performance are beginning to pay off. Apart from lowering labour costs still further, Germany can strive to be more competitive only through innovation and improved conditions for investment. A perceived “innovation gap”, which is closely linked to failings in education and research, has attracted much more atttention in recent years. Academics and business analysts have pointed out the Germans remain excellent at inventing things, but are far less effective at perfecting them and bringing them to market. Germany has been hostile to technology, says Ludolf von Wartenberg, managing director of the BDI, Germany's Industry Federation, and has missed out, for example, on both green (agricultural) and red (medical) biotechnologies. “It has to do with our education system,” says Mr von Wartenberg. “We need an *Aufklärung* (an age of enlightenment).”

This is where he believes politics can make a difference. In 2004 Chancellor Gerhard Schröder formally launched an initiative with leading companies, dubbed “partners for innovation”. Various working groups have been set up, including ones for stimulating new approaches to information technology, specialist materials, education, energy conservation, computerising health services and harnessing venture capital and state aid. Some of these groups have begun long-term projects that will survive any change of government that results from next month's election. And there is money available to publicise the long-term importance of innovation for the economy.

Of course, encouraging economic signs do not mean that Germany has conquered its big structural problems. Studies by research institutes dotted around the country point to the need for tax and

pension reform and solutions to a looming demographic problem. “More babies—preferably this instant!” was one alarm call that graphically illustrates the problem: 1.3m births in 1960 but only 700,000 in 2004. The Berlin Institute for Population and Development proposes that 10% of the women born in the 1960s, now aged 35 to 45, should have an extra child in order to strengthen the number of wage-earners who will be needed to support their generation in retirement.

Both former West Germans and East Germans have been accustomed to a high level of social security and health care. New charges for medical registration, introduced last year, alerted them that things are changing. Warnings that state-sponsored pensions will fall short are beginning to force people to buy, reluctantly, private pension schemes.

But that extra saving does little to help prospects for a consumer-led recovery. A good half of German households are already sitting on abundant wealth if their house ownership is taken into account, which it is not by the German Institute for Retirement Provision, notes a recent article in the weekly *Die Zeit*. If Germans just felt richer, like Americans, they would surely borrow and spend more. Some economists have been urging changes that would make it much easier for Germans to borrow.

Not enough demand

That is because Germany's biggest problem, on which economic recovery could yet founder, is its lack of domestic demand. Unless consumer confidence rises, some analysts argue, there remains a risk that Germany might fall back into a deflationary spiral. Some think higher wages offer a solution. On August 8th Mr Schröder urged German businesses that were doing rather better to give their workers a “decent swig from the bottle”. Peter Bofinger, a member of the *Sachverständigenrat*, the government's independent economic council, believes that wages should be allowed to rise by 2% to 3%. Dirk Schumacher, an economist at Goldman Sachs, an investment bank, argues that size and economies of scale should allow large efficient companies to charge more, pay better and still remain globally competitive.

However, the real issue, says Mr von Wartenberg of the BDI, is to separate wages from ancillary costs such as social security. He fears that one possible move in that direction—a 2% increase in value-added tax proposed by the Christian Democrats—will be squandered by regional governments that want to balance their budget deficits.

Hans-Werner Sinn, head of Ifo, a Munich-based economic research institute, points out that Germany is battling the consequences of five economic shocks: globalisation; the European Union and its enlargement; the introduction of the euro; the opening up of central and eastern Europe; and German re-unification. Each one of these big events has been good for the world as a whole, but has posed particular problems for Germany. It is perhaps remarkable that the country has weathered so many unanticipated blows so well, a tribute to the economy's resilience.

As the biggest economy in the euro zone, Germany has a double straitjacket that prevents it from stimulating a consumption-led boom: interest rates set by the European Central Bank, whose concern is curbing inflation throughout its region, and a stability and growth pact that inhibits countries from borrowing and spending their way out of trouble. Zero-growth, however, is not acceptable politically, even if it were economically.

Government help is also needed to sort out Germany's biggest black hole, the former East Germany now known as “the new *Länder*”. It was a political decision to reunite West and East Germany within a year of the Berlin wall coming down in November 1989. To smooth the deal and to avoid an exodus of East Germans to the west the government made huge transfers, including a *pari passu* pension and social-security system and comparable wages: within four years wages were approaching North American levels. Tax incentives created a construction boom followed within three years by a bust from which the region is still trying to recover. It has left east Germany's poorer *Länder* with over 20% unemployment and few prospects of attracting significant investment.

The multiplier effect

Saxony and parts of Thuringia have become hubs for auto manufacturers and suppliers, and Saxony has also attracted semi-conductor manufacturers. Another former industrial region, Saxony-Anhalt, has high unemployment, but can boast a cluster of chemical firms. Mecklenburg-Pomerania has little but agriculture, some shipbuilding and tourism potential. Brandenburg has seen some ambitious investment projects fail. The upshot is a region that in total still requires transfers of around €90 billion per year, or

4% of the country's GDP. In addition to the unemployed, some 850,000 workers have jobs that depend on the transfers.

Yet the worst aspect, according to Ulrich Blum, head of IWH, a research institute based in east Germany, is that hardly any companies have their headquarters in the region. Successful companies that originated in the east have tended to move their headquarters west. This is a phenomenon not experienced by other central European or even former Soviet countries. The result is east German cities that lack a business elite and, worse still, their high-spending wives and families. Among the few exceptions is Jenoptik, an optical company in Jena. DHL, a subsidiary of Deutsche Post, recently decided to move its logistics hub to Leipzig. Mr Blum told an EU delegation in Dresden recently that the dearth of headquarters was costing the region about 30% of the value-added that companies usually bring.

Mr Blum has a proposal for the region's development that would reward companies for investing there and subsidise research and development. It would focus on smaller successful companies to ensure that they developed the critical mass to survive and grow. This is in contrast to the federal government's "watering-can" approach which has tried to distribute benefits evenly. The current federal approach won't get the private sector investing, claims Mr Blum. It makes more sense to put money where it can have the most impact. And yet even this would not be a quick fix. It will take the new *Länder* 15 to 20 years to get to the level that Bavaria is at today, says Mr Blum. If Germany's politicians make sure that today's foundation for future growth is built on, not undermined, it might just happen sooner.

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Japan's markets

The bulls are back

Aug 18th 2005 | TOKYO
From The Economist print edition

Despite all the political uncertainty, investors are optimistic about Japan

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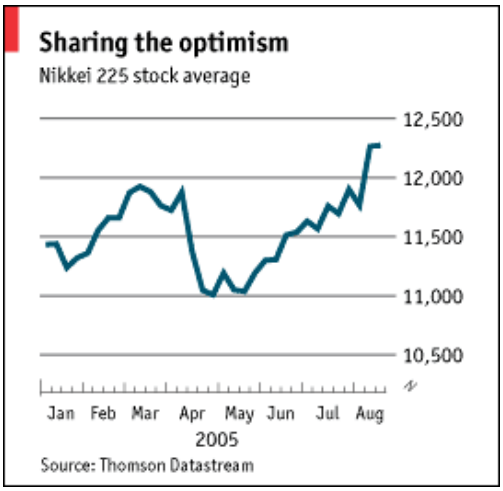

A FEW weeks ago foreign investors were dreading a vote in the upper house of Japan's parliament. If Junichiro Koizumi's post-office privatisation package failed, and if the prime minister then called a snap election, economic reform would suffer a double blow. Both these things duly happened on August 8th. Yet investors don't seem too bothered after all. A string of nice economic figures this summer—like last week's on machinery orders, wholesale prices and domestic demand—has simply been too good to ignore.

The Nikkei stockmarket index, which slid the week before the post-office vote, climbed by 5% the week after. It has gained 14% in three months, to a four-year high (see chart). The yen is perky too, up by 2% in the past fortnight: a dollar now buys around ¥110. Falling bond prices in the past two weeks have rounded out the bullish trifecta. (That said, with yields on ten-year government bonds at only 1.4%, it is still not hard to pick the deflationary economy out of a rich-country line-up.)

Japan bulls have been disappointed many times before. Might they be again? One reason for caution is that foreigners have been doing all the buying, while locals have sat on their hands. Another is that the naysayers have sensible arguments as well as history on their side. Take Morgan Stanley's Robert Feldman, who has been among the most bullish observers of Japan in the past couple of years but now calls himself a “party pooper”. Mr Feldman has been impressed with Mr Koizumi, giving him high marks for economic reform and predicting stellar results if the prime minister pushed more of his plans through. Now that there is a threat of gridlock after the general election on September 11th, says Mr Feldman, all that Mr Koizumi was working for is at risk—and so are the prospects for growth.

Still, investors are scarcely ignorant of the risks: having suffered many wounds in the past decade, Japan bulls no longer charge at the first wave of the red cape. It is just that the steady accumulation of good news has gradually led them to shake off some doubts about the world's most frustrating economy. Last week, for instance, it was reported that GDP grew at an annual rate of only 1.1% in the second quarter, less than expected. The optimists concluded that, on close inspection, the figures were not that bad. Growth was slow, yes, but mainly because inventories fell. That's a good sign, said the bulls, because manufacturers are now burdened with fewer unsold goods. And perhaps more important, the GDP figures seemed to back up other evidence that the recovery is broadening beyond exports and capital investment, to include consumption.

A tightening job market may help to sustain this trend. In the first stage of its recovery, the Japanese economy created lots of part-time and temporary jobs; since the start of the year, full-time employment has been on the rise. In the year to June, it grew by 1.1%. There are now more job offers per applicant than at any time since 1992; unemployment has fallen to 4.2%, from 5.5% in early 2003. Moreover, since profits are strong and global demand looks fairly healthy, investors are a little less worried that exports and capital investment will stagnate before domestic demand can take up the running.

By Japan's standards, all of this amounts to a pretty scene. In early August, *The Economist*'s poll of forecasters was predicting that real GDP would grow by 1.7% this year and next, and that consumer prices would rise—at long last—by 0.3% next year. Many economists have raised their growth forecasts since then. Yes, Japan has disappointed often, and September's election is important. But the economic

climate has not been this sunny in a while. Let the bulls have a little fun.

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Arab investment

Pumped up

Aug 18th 2005
From The Economist print edition

Saudi Arabia's stockmarket soars

LARGE and liquid aptly describes Saudi Arabia's greatest natural resource—its oil reserves. But it applies equally to the kingdom's booming stockmarket. The Tadawul All-Share Index has risen by more than 70% this year. With a market capitalisation that exceeds $500 billion and an average daily turnover of more than $2 billion, it is now the biggest emerging stockmarket in the world, according to analysts at HSBC. (Their definition excludes Hong Kong, which is worth more.)

Rising oil prices are fuelling this growth, helped by low interest rates and, after September 11th, 2001, a growing desire among Arab investors to keep their money in the region. And there is more for them to invest in, as economies diversify and state-owned assets are at least partially privatised.

The Saudi market has already seen four initial public offerings this year and more are on the way, helped by new capital-market laws designed to bring more rigour to the system. Future flotations are expected to include Saudi Research and Marketing Group, a publisher whose titles include *Asharq Al-Awsat*, a leading Arab newspaper, and almost a dozen insurance companies.

Valuations are high. John Lomax, a strategist at HSBC, reckons that the Saudi market will trade on a 2005 price/earnings multiple of almost 35, more than double that of leading emerging markets outside the region. But there is strong underlying growth in the operations of many listed companies, says Walid Shihabi, head of research at SHUAA Capital, an investment bank in Dubai. For example, SABIC, a petrochemicals company whose partial free float (70% of the shares are owned by the Saudi government) accounts for almost 30% of the stockmarket's value, is doing well on the back of a relatively low cost base and rising global demand for its products.

A correction is likely eventually, but for now, with oil prices high, the good times continue. It is hard for outsiders to join the party, however. Less than 5% of Saudi shares are owned by other Gulf investors, who are prohibited from investing in banking and insurance stocks; foreigners from further afield cannot invest directly in the market, though they can get a look-in by putting their money into, say, Saudi mutual funds.

But at these valuations, would they want to? The problem with the Saudi market, according to Edmund O'Sullivan, editorial director of the *Middle East Economic Digest,* is too few investment opportunities for all this money. Many of the country's best companies are still private, family-owned concerns. For public investors, that is one deep well that cannot be tapped.

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Stock exchanges

Bouncer

Aug 18th 2005
From The Economist print edition

An Australian firm shows interest in the London Stock Exchange

AUGUST is supposed to be a quiet month in Britain, when the pulse of life slows and thoughts turn to the beach. This month, however, Australians are stirring things up, both on the cricket field (where the English and Aussie national teams are playing a nail-biting series) and in the City of London. This week Macquarie Bank, of Sydney, said it was mulling an offer for the London Stock Exchange (LSE). The exchange has no lack of admirers. After rebuffing Deutsche Börse, which among other things runs the Frankfurt stockmarket, it is still being wooed by Euronext, another continental European rival. And this week the name of OM, a Nordic exchange operator that bid unsuccessfully for the LSE a few years ago, surfaced again. The LSE, however, insists that it is quite happy being independent.

It is unclear whether Macquarie is truly serious about making a move for the LSE. The bank has said that a formal offer for the exchange, if it makes one, will be with a consortium, and probably for cash. Macquarie has an unconventional business model, ranging from investment banking to private equity, fund management and financial advice. Its ever-expanding holdings range from toll roads, utilities and gold mines to BBC Broadcast, the European multimedia service of Britain's oldest broadcaster, which it acquired in June. It is also said to be contemplating the purchase of Taiwan Broadband Communications, a cable operator, for about $700m. It usually spins off new assets into specialist funds, most of which are listed. At the end of March, it had assets worth A$88.9 billion ($69 billion) under management, 42% more than a year before. So far, it has not added a stock exchange to its collection.

Many analysts have reacted coolly to the prospect of the Australian bid, saying that Euronext remains a more attractive match for the LSE. They like the thought of tying London to Euronext's stock exchanges in Amsterdam, Brussels, Lisbon and Paris, and to its Liffe derivatives business. The pan-European group is likely to go ahead with its bid, while trying to satisfy regulators who have concerns about its clearing holdings.

Still, an offer from Macquarie would not be so unusual. Exchanges have attracted private investors before. This week it was reported that Blackstone and General Atlantic, both private-equity firms, and Battery Ventures, a venture-capital firm, may jointly bid for a stake in the New York Mercantile Exchange (Nymex). Blackstone previously invested in Liffe. General Atlantic is a key shareholder in Archipelago, an electronic exchange that is due to merge with the New York Stock Exchange. Apax Partners, another private-equity firm, was a founder of EASDAQ, later part of NASDAQ Europe.

Whether such investments are wise depends upon how efficient an exchange has become, says Benn Steil, an expert on exchanges at the Council on Foreign Relations, a New York think-tank. Blackstone's interest in Nymex makes sense, he contends, because “there's a lot of reform to beat out of that organisation”, which is still member-owned. “Blackstone want to be part of the reform process.” The LSE, on the other hand, has changed dramatically since the late 1990s, gaining efficiency and diversifying its shareholder base.

Despite such doubts, Macquarie cannot be ruled out. “Our general pattern is to buy and hold” assets, says Allan Moss, the chief executive. He adds that Macquarie is “generally an active, hands-on investor, though we don't always seek to have a leading role.” In previous acquisitions, it has shown itself ready to find partners with relevant expertise.

A deal with another exchange operator, though, could bring the LSE a partner with a big derivatives business, which it lacks. “Equities is a solid business, but your growth is limited to new companies listing,” says Mr Steil. “With derivatives you're limited by your imagination.”

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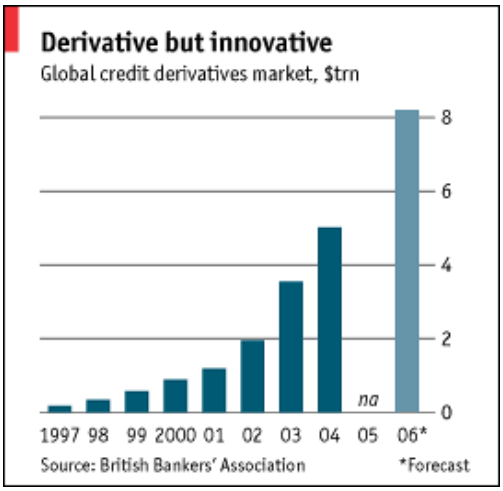
Credit derivatives

Risky business

Aug 18th 2005
From The Economist print edition

The market for insurance against credit default continues to boom



WHAT do Delphi, a huge auto-parts company, Northwest Airlines and Delta, another airline, have in common? All three American companies are fighting hard to avoid filing for bankruptcy. There was a time when those who had lent money to such firms would have watched events nervously. Today, it is unclear who exactly is sweating.

The reason is the proliferation of credit derivatives—contracts that let lenders shift the risk that a company will default on to another party for a fee. So a bank lending to Delphi, say, could pay a premium to another financial institution (perhaps a pension fund or an insurer, or another bank) to take on the risk that the parts maker will be unable to meet its obligations.

A decade ago, credit derivatives barely existed. Now the market for them is big, and still growing fast. The British Bankers' Association, which carries out a survey every couple of years, reckons that the global market hit $5 trillion last year and that it will pass $8 trillion in 2006 (see chart).

So far, credit derivatives seem to have been healthy for the banking system. By enabling the unbundling of financial risks (splitting, say, the interest-rate and credit risk in a corporate bond), they have allowed finer tuning of risk management. Alan Greenspan, chairman of America's Federal Reserve, has attributed the resilience of his country's banks in 2001 and 2002—when Enron, WorldCom and the Argentine government defaulted—to credit derivatives, which spread the burden of the defaults across a broad group of banks and other institutions.

The market's development has been helped by the increasing standardisation of credit-derivatives contracts. And new investors have been attracted by the creation of standard products based on credit derivatives, such as indices that offer exposure to, or hedges against, pools of risk (eg, European or Japanese corporate credit).

Sold by the slice

But perhaps most important has been the growth of complex products that appeal to yield-hungry investors. The first credit derivatives were fairly straightforward “credit default swaps” that transferred the credit-default risk of a single company. But the lion's share of recent growth has been in the “tranched” market. Here, in essence, pools of credits are sliced into riskier and less risky bits (or tranches) and sold. So, for instance, a risk-averse investor could choose to buy the tranche that exposes him to credit risk only after the first 10% of credit losses have been absorbed by other investors. An investor with a bigger appetite for risk and yield would buy this first slice. “In a lowish interest-rate environment, with tight credit spreads, investors are desperate for yield—and tranched instruments are a way for investors to get juicier returns,” says one bank regulator.

Of course, things can go wrong. It is possible that the pricing of ever more complicated instruments might sometimes be too much even for the ultra-brainy lot who do it, with expensive results. Tranched instruments have no clear market price, so they have to be valued with complex models. Working out whether a default in a portfolio is likely to be an isolated event, or is a harbinger of more to come, is especially tricky, not least because data on credit defaults are relatively sparse.

Some worry about the increased activity of hedge funds which, lured by the yield on illiquid, complicated instruments, make up as much as 70% of trading volume in credit derivatives, by some counts. Mainly, this concern revolves around newer funds that lack experience in managing complicated risks. Their inexperience might increase counterparty risk—the danger that a seller of credit protection cannot pay in the event of a default. The worry is exacerbated by the high leverage (ie, use of borrowed money) of many hedge funds: this boosts returns on good days but magnifies losses too.

So far, though, there have been no big problems. Some hedge funds lost a lot on credit derivatives after the debt of General Motors was downgraded earlier this year, but these troubles were isolated. They may even have been a good thing: a salutary reminder of the risks.

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Economics focus

Destitution not dearth

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Niger's harvest last year was not so terrible. Why is the country now so hungry?

"MUCH about poverty is obvious enough," wrote Amartya Sen, one of the world's best-known and most respected economists, in his 1982 classic, "Poverty and Famines". "One does not need elaborate criteria, cunning measurement, or probing analysis to recognise raw poverty and to understand its antecedents." But the thesis Mr Sen propounded in that book was not obvious at all: some of the worst famines, he argued, have taken place without any significant fall in the supply of food.

One of the examples Mr Sen chose to illustrate his thesis was a famine that gathered force from 1968 to 1973 in the Sahel region of Africa. The Sahel, from the Arabic word for "shore", typically refers to a group of six countries on the western fringes of the Sahara, where the desert sands lap up against the vegetation of Africa's semi-arid zones. The countries worst affected by this disaster 30 years ago were Mauritania, Mali, Upper Volta (now called Burkina Faso)—and Niger.

Niger is once again in the grip of a food crisis, if not a full-blown famine. The distress sales of livestock, the heavy migration and the deprivation the country suffered in the early 1970s have all revisited it again this year. How well does Mr Sen's thesis explain the country's latest encounter with mass hunger?

Much about Niger's current crisis appears obvious enough: the rains last year ended early; the locusts were rampant. Who can be surprised that the country is short of food? But Niger's harvest last November was merely mediocre, not disastrous. Although the rains ended early, the country's cereal production was only about 11% below its five-year average, according to the UN's Food and Agriculture Organisation (FAO). It was 22% greater than the harvest of 2000-01, a year that passed without alarm. The locusts did more damage to the region's fodder than to its food, prompting pastoralists and their herds to begin an early migration to greener pastures in Niger's coastal neighbours.

Purchasing powerlessness

Niger's distress shows up most clearly in prices, not quantities. A pastoralist's terms of trade depend on two prices in particular: the price of what he can sell (his livestock) and the price of what he must buy (food). In Niger this year, the latter has soared; the former has plummeted. According to one report, the price of millet and sorghum rose to 75-80% above its average for the last five years. By June, the sale of one goat bought half as much millet as it had six months earlier. It is precisely this kind of cruel twist in the terms of trade, Mr Sen argued, that can bring a community to its knees. These unfortunates will suffer a lack of power to purchase food, even if there is no lack of food to purchase. Why did prices move against Niger's pastoralists so far and so fast?

The spike in the food price may have reflected high foreign demand as much as low domestic supply. Traditionally, during the lean months before their harvest, Niger's farmers import cereals that are cheaper to grow in wetter, coastal neighbouring countries than in their own country. But according to CILSS, an intergovernmental body responsible for the region's food security, significant amounts of grain have this year been flowing in the opposite direction. Ghana, Benin, Côte d'Ivoire and Nigeria have all been buying up grain in the region.

This is partly because these countries' own harvests were disappointing. But in Nigeria's case, the FAO thinks that government policies were also to blame. Nigeria has imposed controls on imports of rice and wheat products; it has also taken steps to protect and promote its millers and poultry farmers. Both of these policies have raised demand in the country for millet and sorghum, which provide alternative sources of flour as well as chicken-feed. As a result, Nigerian cereals that might have found their way to Niger are instead being consumed at home. Nigeria has twice Niger's income per head and more than

ten times its population. Its powerful market pull may have helped to undermine the purchasing power of Niger's pastoralists. “In the fight for market command over food,” Mr Sen noted in his book, “one group can suffer precisely from another group's prosperity, with the Devil taking the hindmost.”

Nigeria, with Burkina Faso and Mali, has also restricted grain exports to Niger this year, violating its trade treaties with the country. Such restrictions have often played an ignoble, supporting role in the history of famine. A ban on cereal exports between India's provinces, for example, condemned Bengal to ruinously high prices in its great famine of 1943.

What of the other term in the terms of trade? Livestock prices have fallen in the past year, partly because northern pastures were damaged and animals were emaciated as a result. But the deterioration in the terms of trade can also generate its own momentum. Higher cereals prices prompt herdsmen to sell more of their livestock. These distress sales drive the price of animals down further, forcing pastoralists to sell still more of their herd. In his book, Mr Sen raised the theoretical possibility that a pastoralist's supply curve might actually bend back on itself: as the relative price of livestock falls, a hungry pastoralist might supply more animals to the market, not fewer as elementary economic principles would imply.

If mass hunger were simply the result of there not being enough to eat, the remedy would be obvious: more food. The emergency rations now being shipped, flown and trucked into the Sahel are indeed necessary and urgent by the time hunger and destitution are acute and widespread. But if mass hunger begins with a collapse in purchasing power, rather than a shortage of food, it does not take an airlift to prevent it. What is needed is a way to restore lost purchasing power by, for example, offering employment, at a suitable wage, on public works. The market respects demand, not need. But give the needy enough pull in the market, and the market will do most of the rest.

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Conservation

Back to the future

Aug 18th 2005
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Michael Long - NHMPL

Conservationists tend to be conservative. But not always. Here is one strikingly non-conservative conservation idea

PEOPLE and wildlife don't get on too well together. Large mammals, in particular, have a hard time at the hands of humanity. Their habitat gets taken for farms, their bodies for dinner and their heads for trophies. As human populations grow, the pressure increases, and it seems to decline only when people are rich enough to focus on the aesthetic as well as the economic possibilities of wild beasts. Often, such aesthetic appreciation thrives best in the safety of the city rather than in the rawness of the wilderness.

Observing all this, a group of conservation biologists, led by Josh Donlan of Cornell University, have made a modest proposal in this week's *Nature*. They suggest a piece of ecological arbitrage.

Africa and Asia are continents where wildlife is under particular pressure. Their human populations are growing and their people are not yet prosperous enough to make conservation a higher priority than simply getting by in life. But many of the world's endangered mammals live in Africa and Asia. In North America, by contrast, rural populations are shrinking, people are rich enough to care about wildlife, and many of them do. Moreover, most of the large North American mammals that existed when humanity arrived in the continent are now extinct. When the first immigrants entered North America at the end of the Pleistocene epoch, more than 13,000 years ago (how much more is the subject of vigorous debate), they found a continent full of large mammals—elephants, lions, cheetahs, camels, horses and more. Within a few thousand years most of these animals were gone, probably the victims of overhunting. Their ecological niches are therefore wide open for occupation. What could be more logical, Mr Donlan suggests, than introducing endangered Old World mammals into the New World, thus saving them from extinction while returning wild America to something like the state it was in before *Homo sapiens* took up residence?

Pleistocene park

Mr Donlan's plan is to create game reserves of a quarter of a million hectares or more in the Great Plains of North America, and populate them with a mixture of native American and alien animals. If returned to grassland (not a stupid idea, as the government now pays farmers large sums not to grow crops on quite a lot of them) the plains could support both grazers and their predators. Beginning gradually on small, private reserves, wild horses, asses and camels would be introduced and biologists could study

their effects on the ecosystem. Later, if all had gone well, elephants would be added and finally, to provide predators, big cats. If everything worked on a small scale, the large public nature reserves envisaged as the plan's culmination would then be created. Mr Donlan reckons that the whole process would take about 50 years. “It is important”, as he puts it, “to realise that we're not advocating backing up a van full of cheetahs and kicking them out the door.”

Although none of the animals Mr Donlan and his colleagues propose introducing are the same species as the ones that went extinct, many are related and all would fill similar ecological niches. Elephants, for instance, would help to preserve the grassland by eating shrubs that encroach on it—a role previously filled by mastodons (pictured above). Lions and cheetahs would control the populations of horses, asses and camels much as their sabre-toothed cousins once controlled similar ungulates. Cheetahs would also act as predators of pronghorn antelopes, which can outrun anything around at the moment, and whose speed is suspected to be an evolutionary response to the North American cheetah, now extinct.

In theory, the return of the big mammals would result in more diversity throughout the ecosystem. It would also, the researchers suggest, bring tourists flocking to the Great Plains and provide an alternative income for people there. That may sound fanciful. But, as Mr Donlan's paper points out, there are already some 77,000 large exotic mammals, most of them African or Asian species, roaming freely on private ranches in Texas and, in some cases, attracting paying customers.

Many mainstream conservationists are naturally (in more than one sense of that word) suspicious. Chris Haney, a conservation biologist at Defenders of Wildlife, a voluntary conservation group, fears the effort might detract from what he describes as “more realistic” goals, such as the reintroduction of wolves, bison, grizzly bears and North American elk (not to be confused with the European sort, known to Americans as moose). These reintroductions have faced bitter opposition from some ranchers, farmers and politicians. In Yellowstone National Park, a wolf-reintroduction programme begun in 1995 was ultimately successful, but not before a number of lawsuits were heard, thousands of dollars paid to ranchers for lost livestock, and two of the wolves illegally shot. If programmes like this were seen not merely in isolation, but as the first steps in a grand plan to reintroduce lions and cheetahs, they would be even harder to implement.

Eric Dinerstein, chief scientist at the World Wildlife Fund US, another conservation charity, has a related objection. He suggests Mr Donlan's idea might be damaging not only to efforts to conserve North American species, but also to the very Old World species it is intended to save. He thinks Mr Donlan is too pessimistic about the chances of preserving endangered animals in their African and Asian homes. Rather than spending money to establish those species in North America, Dr Dinerstein would prefer to see it spent conserving them where they live now.

Both of these objections are sensible, though not overwhelmingly so. But Dr Haney has a more visceral worry, too. Modern conservation is generally against the idea of species being spread into novel habitats, and he opposes Mr Donlan's idea on those grounds, as well.

One reason conservationists try to stop alien introductions is pragmatic—they sometimes do serious damage to native species. Rats, cats and pigs, for example, have wrecked the native fauna of many a small island. But part of the objection to alien introductions has an ideological flavour. There is a feeling that what exists now (or, at least, what existed before man stuck his oar in) is what *ought* to exist. It is pristine. Shipping in other species is, in a sense, a form of pollution.

Perhaps it is, although such pollution does happen naturally from time to time. But even if such introductions are not the ideal solution, they may be the best one available. Mr Donlan's idea is a big and imaginative proposal to solve a clear and present danger. It is certainly worth some careful scrutiny.

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AIDS

Prostitution v constitution

Aug 18th 2005
From The Economist print edition

A challenge to America's anti-AIDS policy

Get article background

SINCE it was announced in 2003, PEPFAR, America's $15-billion aid package to help fight AIDS abroad, has stirred up a storm over its socially conservative stance on such issues as sexual abstinence and condoms. The latest controversy is over commercial sex work, as prostitution is delicately known in the AIDS-prevention community. DKT International, a social-marketing organisation that supplies condoms and other family-planning goods in the developing world, has sued USAID, America's foreign assistance agency, for requiring it to sign an “anti-prostitution pledge” in order to receive funds. DKT regards this restriction as not only detrimental to the global fight against the disease, but also a violation of its constitutional right to free speech.

According to the congressional legislation that covers PEPFAR, government funds may not be spent on activities that promote or advocate the legalisation or practice of prostitution and sex trafficking. Nor may this money be used to assist any group or organisation that does not have an explicit policy opposing prostitution and sex trafficking. DKT says it lost $60,000-worth of funding for a condom project in Vietnam, with the prospect of larger funding losses to follow, when its local representative refused to accept the latter requirement.

Phil Harvey, the head of DKT, argues that the government's policy undermines the battle against AIDS by forcing groups to condemn the very people they seek to help—commercial sex workers at high risk of catching the disease. This is hardly the basis of a trusting, effective partnership to prevent the spread of AIDS.

Moreover, the policy does not clearly define what it means by prostitution. Does it include, for example, so-called “transactional sex”, when women exchange favours for food or clothing and which is a fact of life in many developing countries? Nor does it make clear what “opposing prostitution” means in practice for a group receiving American government money. “No one pretends that such a policy will contain or ameliorate the darker aspects of the world's oldest profession,” says Mr Harvey. “Rather it represents posturing by American politicians who are increasingly seen around the world as patronising, bullying and obsessed with sex.”

This is not the first time that sex has put American foreign-development aid in a twist. In another controversial piece of legislation, the “Global Gag Rule” as its critics call it, government money cannot be given to foreign non-governmental organisations (NGOs) that perform or actively promote abortion as a method of family planning, even if the money they are using to do so comes from other sources. (America has long banned the direct funding of abortion services abroad.) But the Gag Rule does not apply to American NGOs because it was deemed a violation of the right to free speech.

The requirements for anti-prostitution policies in the current AIDS legislation are being applied to both foreign and American groups, however, after a letter from the Department of Justice late last year said that “there are reasonable arguments to support their constitutionality”. DKT and others, including lawyers at the Brennan Centre for Justice at New York University's School of Law, disagree. Hence DKT's case against the government for a violation of its First Amendment rights.

Jodi Jacobson, the head of the Centre for Health and Gender Equity, an American advocacy group, worries that if DKT loses its case, then conservatives in the government might have another go at trying to apply the Gag Rule to domestic groups. Things should be a little clearer in a month or so, when Mr Harvey expects a court decision on DKT's application for a preliminary injunction against USAID. This injunction, if granted, would prevent the agency from applying its anti-prostitution policy until the full case is heard, which could take more than eight months.

Mr Harvey, who has a long history of challenging government on free speech and other issues, with several wins to his credit, says he will stay with the case all the way to the Supreme Court. Many of those working in international public health and sexual rights hope that he can add this one to his list of victories.

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Paying attention

Cor blimey

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Gory and erotic images can affect your vision

IT'S true. Pornography can make you blind. Look at a smutty picture and, according to research by Steven Most, of Yale University, and his colleagues, you will suffer from a temporary condition known as emotion-induced blindness.

Dr Most made this discovery while studying the rubbernecking effect (when people slow down to stare at a car accident). Rubbernecking represents a serious lapse of attention to the road, but he wondered if the initial reaction to such gory scenes could cause smaller lapses. The answer is, it does. What he found was that when people look at gory images—and also erotic ones—they fail to process what they see immediately afterwards. This period of blindness lasts between two-tenths and eight-tenths of a second. That is long enough for a driver transfixed by an erotic advert on a billboard to cause an accident.

The researchers conducted two experiments. In the first, the results of which will be published in next month's *Psychonomic Bulletin and Review*, the experimental subjects were shown a sequence of images. Some of these images were gory (violent injuries and mutilated bodies) while others were photographs of landscapes and buildings—things thought to be emotionally neutral. The subjects were asked to watch out for a picture that had been rotated, without being told what was in it. Between the horror picture and this target were two to eight neutral pictures. The closer the grim picture was to the target, the less likely the subjects were to spot the target. When the gory pictures were substituted by erotic ones, the outcome was the same.

Dr Most thinks that the explanation for this temporary blindness is that there is an information-processing bottleneck in the brain when it is presented with important stimuli. When the human brain was evolving, such stimuli would not have been two-dimensional images. They would, rather, have been part of the real world. Gory scenes would have had survival value (ie, “am I going to be next?”), while erotic ones would have had reproductive value. Paying attention to the landscape would have been a distraction.

In the age of photography, though, it is the image that is the distraction, and if the distracted individual is travelling at speed in a car, such distraction could be fatal. So the team carried out a second series of experiments, still unpublished, that were intended to discover whether their subjects could override this emotion-induced temporary blindness by using what they rather grandiloquently called an “attentional strategy” (ie, focusing harder on the target image). This was arranged by asking the subjects to find not any rotated photo, but a rotated photo of a building, in the array of images. The fact that they had to pay attention to both content and orientation meant they focused harder. As the researchers had expected, in this version of the experiment subjects were, on average, better at spotting the target image.

But that average concealed some interesting differences that depended on a subject's personality. The researchers knew from previous studies that the more neurotic someone is, the worse he is at controlling his attention, so they decided to see how a measure of neuroses known as the harm-avoidance scale correlated with their results. The harm-avoidance scale is a measure of a person's reaction to negative or frightening stimuli. They found that the lower a subject's score on this scale was, the more successful he was at detecting the target. This information might be useful when considering the reliability of witnesses to crimes.

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Robotics

Dermatology for 'droids

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Researchers manufacture electronic skin for the robots of the future

ROBOT brains are getting smarter, and are likely to continue doing so for some time to come. While it would take several hundred of today's Pentium chips to supply as many transistors as the human brain has nerve cells, in 15 years it should take only one or two of the Pentium's successors to do the job. But the brain, while certainly the human body's most intricate and complex organ, is not its largest. That honour belongs to the skin—all two square metres and ten or more kilograms of it. The skin not only protects the body, the senses in it also tell the brain a lot about what is going on in the outside world. So, as man seeks to create a robot in his own image, he will need to find something for the outside to cover the Intel inside.

This week, a group of researchers led by Takao Someya of the University of Tokyo announced in the *Proceedings of the National Academy of Sciences* that they have taken a step towards providing such a covering. The team has fabricated flexible webs of plastic that include temperature and pressure sensors and are suitable for use as “E-skin” for robots.

The key to the team's technique is the use of transistors made from organic semiconductors. Unlike traditional semiconductors, which are crystals of elements such as silicon and germanium, organic semiconductors are more complex versions of the chemicals from which plastics are made. While organic semiconductors are not as good as their inorganic cousins for high-performance computing, they can be processed at lower temperatures, which means that they can be deposited on to plastic bases that would melt if traditional semiconductors were used.

Dr Someya's E-skin consists of two layers laminated together. In one, sensitive to pressure, each transistor is connected to a conductive rubber pad whose electrical resistance changes when it is squeezed. In the other, sensitive to temperature, the transistors are connected to diodes made from two different organic semiconductors. As the temperature changes, so does the voltage measured across the diode.

To prove that E-skin is suitable for something like a robotic fingertip, the team stretched it to cover the top half of an egg. In addition, they pressed a small copper block that was kept at a temperature of 50°C against it. They were able to obtain simultaneous images of both the pressure and the temperature distribution “felt” by the skin.

With further technological advances, electronic skin like this could give robots more than just the human range of senses. The researchers point out that sensors for such things as humidity and ultrasound (for sensing how close the robot is to another object) could be embedded in the mesh, giving robots of the future sixth or even seventh senses.

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Jewish history

Facing Zion

Aug 18th 2005
From The Economist print edition

EPA

A new history of the Jews is anxious about Israel, less so about Jewish identity

MOST popular accounts of the Jewish story manage to resolve its tragedy and heroism into a chord of triumph. Not so Howard Sachar's new history, which avoids the redemptive line taken in books such as Paul Johnson's "A History of the Jews", published almost 20 years ago.

In part, this is because of the slice of time that Mr Sachar has chosen. His history begins in the 18th century, when Jews were a barely tolerated minority in most of Europe; they were taxed, along with honey, hops, chalk and charcoal, if they wanted to enter the city of Mainz. It ends not in celebration, with the founding of Israel, but with anxiety, both about its future and about a possible revival of anti-Semitism in Europe. In between lies a long tale marked by brilliance and catastrophe.

A History of the Jews in the Modern World
By Howard M. Sachar

Knopf; 830 pages; $40

Buy it at
Amazon.com
Amazon.co.uk

Mr Sachar, a respected emeritus professor of history at George Washington University, thus compounds the problems inherent in retelling Jewish history. Jews as a people were acted upon more often than they were capable of acting. Their great men and women often found greatness in forgetting, rather than embracing, their Jewish origins. Mr Sachar rises to the challenge in some ways, though not all. When dealing with the outrages perpetrated against Jews he lets the facts speak for themselves. But when Jews oppress each other or wallow complacently in good fortune, he is quick to note it. Tsar Nicholas I pressed Jewish boys into the Russian army, but the *khappers* who snatched them from their homes at night were functionaries of the Jewish community. Jewish day schools became popular in America in the 20th century, writes Mr Sachar, not least because they offered Jews a face-saving way of avoiding racial integration.

Giants, such as Moses Montefiore, a Victorian tycoon, are given their due. Among the book's pleasures are also portraits of lesser-known figures. Gabriel Riesser, a 19th-century German patriot, frequented cafés that did not welcome Jews and, unless served, would sue their owners. Mr Sachar is determined to leave no Jewish community behind, offering chapters on Jews in Latin America and the British

Commonwealth. Buffeted by most of the storms of the past three centuries, Jews coped with bigotry, left when they had to and flourished when permitted.

However, if Zion is not to be your grand finale then you must deal with the fate of Jews as Jews in the Diaspora. And here Mr Sachar's volume becomes afflicted with a strange, fatal fuzziness. It is not that he ignores the dilemma—how to become part of the mix without dissolving—that faced Jews living or hoping to live in tolerant societies; no modern history could avoid it. “Be a man in the streets and a Jew at home/A brother to your countrymen and a servant to your ruler,” urged a Jewish poet in tsarist Russia. Mr Sachar certainly addresses Jewish responses to emancipation and modernity, but he handles them with surgical gloves and a set of tongs. He habitually describes religious Jews as “pietistic”, rather than devout or simply pious. Instead of assimilated Jews we have “acculturated” ones, suggesting that religion is really no big loss and that assimilation is not a threat. Jews will always be Jews no matter what.

This assumption estranges him from some of his material. He notes, for example, that between 1926 and 1939 the proportion of Jews in the Soviet Union listing Russian as their first language rose from a quarter to more than half. Yet he has little to say on the consequences of this colossal shift for the Russian Jews' sense of themselves as Jews. Equally, in his discussion of Jews in America he manages to avoid mentioning that half of them marry gentiles.

Instead Mr Sachar devotes inordinate space to people who happened to be Jewish but made nothing of it, such as the Communist notables, Leon Trotsky (né Lev Davidovich Bronstein) and Béla Kun. He appears to cast his lot with the “matter-of-fact Jewishness” of Sigmund Freud, who made mighty contributions to western culture though he credited his Jewish origins for making them possible. “Do not deprive him of that advantage,” Freud warned a friend who was thinking of converting his son to Christianity.

Readers will be dazzled by a people who stepped out of the *shtetl* and took up the Stradivarius. But, as identity becomes increasingly a matter of choice rather than a fate, there should be more to say about the possible losses, as well as the gains, inherent in a matter-of-fact approach to being Jewish.

A History of the Jews in the Modern World.
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The English scientific revolution

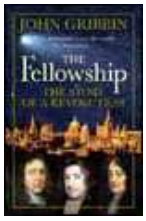
Astrologers and alchemists

Aug 18th 2005
From The Economist print edition

WHEN Giordano Bruno gave a lecture on natural philosophy at the University of Paris in 1585, his audience was so incensed at the liberties he took with long-established principles that he had to escape through a window. A century later, gentlemen were meeting regularly to observe new experiments at the Royal Society in London, under a constitution that banned them from talking about religion or politics. They were doing science in a way that would be familiar to anyone who has ever messed around with springs and weights in a physics lesson. What happened in between is normally called the scientific revolution.

It was a strange kind of revolution; no one talked about it at the time. Despite the neophyte titles of many contemporary works—Galileo Galilei wrote the "Two New Sciences", Johannes Kepler the "New Astronomy" and Francis Bacon the "New Atlantis"—the idea that there had been a scientific revolution in the 17th century did not take hold until the 1930s. Even so, the term has prospered as shorthand for a period of about 150 years that changed the way that people see the world.

The Fellowship: The Story of a Revolution
By John Gribbin



Penguin/Allen Lane; 336 pages; £20

Buy it at Amazon.co.uk

John Gribbin's book tells the story through a series of key events, focusing on England. It begins with William Gilbert busily rubbing lumps of amber and observing their effects on his metal light needle. Mr Gribbin then runs through the greatest hits of Galileo, Robert Boyle, Robert Hooke and Isaac Newton, punctuated with potted biographies of a handful of less well-known figures. The book ends with a chapter called "The Icing on the Cake", a reference to Edmond Halley's successful prediction that the comet he observed in 1682 would return in about 1758—an event that took the innovations in cosmology of the preceding century from the theoretical to the verifiable in one celestial firework.

Calling a final chapter "The Icing on the Cake" is a mistake in any book, unless of course the preceding chapters are about French Fancies. And it is particularly wrong-headed for this story. Although scientists devised beautifully neat formulae to explain complicated phenomena, the scientific revolution itself was a messy business. For a start, some natural philosophers refused to behave like scientists. Newton spent many of his best years working away on theology and alchemy, rather than dutifully laying down the foundations of modern physics. The experiments at the heart of the new philosophical method were often hard to replicate. Boyle's famous air pumps, for example, were always leaking. And by the 18th century, when the revolution really ought to have been over, armillary spheres were still being produced with the Ptolemaic and Copernican heavens side by side, as if the makers had hedged their bets.

Mr Gribbin knows this, but doesn't consider his readers smart enough to understand it. So he dismisses Newton's theology and alchemy as irrelevant, as he does the development of Bacon's musings about natural philosophy. And William Harvey's vivisections, which helped him to understand the circulation of the blood. Mr Gribbin reckons they are "not for the squeamish", and moves on. This is history with much of the story missing.

By the end of the book it is not at all clear why a limited experimental culture did develop in England in the late 1600s. Mr Gribbin's thesis—that the Catholic church had made life impossible for natural philosophers elsewhere, and that "somewhere had to take the lead, and that somewhere was England"—is no help.

The Fellowship: The Story of a Revolution.
By John Gribbin.
Penguin/Allen Lane; 336 pages; £20

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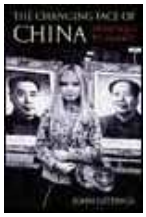
Modern China

Fear of the future

Aug 18th 2005
From The Economist print edition

The Changing Face of China: From Mao to Market
By John Gittings



Oxford University Press; 384 pages; $30 and £18.99

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WHITHER China is arguably the most vital, if the least fathomable, strategic question of the 21st century. John Gittings, a veteran journalist and prolific writer, has produced a new study of China's Communist era and its likely trajectory. Unfortunately, his book will have many readers still scratching their heads.

Mr Gittings is sceptical of the view that China's huge internal stresses—from dysfunctional banks to religious unrest—have pushed it to the verge of catastrophe. Yet his argument is hedged with sufficient caveats that the pessimist could still feel vindicated. “The Chinese miracle is a precarious one: the leadership...only has a few years to get it right,” he suggests. The leadership needs to initiate “serious reforms” of the political structure within this period. But the leadership Mr Gittings describes is one that has a congenital disinclination to reform itself.

The author's biggest concern is about the ravages to China's environment caused by breakneck industrial growth. Environmental degradation and rising pollution, he argues, represent a far more serious threat to the Chinese people than either political or economic instability. He even proposes a nightmare scenario in which China will run out of water. Mr Gittings is altogether too gloomy on this issue. Another, and in this reviewer's opinion, more likely, scenario is that China's huge environmental problems will cause widespread suffering. But they will also become part of the powerful cocktail of emerging challenges to an unreformed party that will force it to change the way it rules.

Increasingly frequent protests, triggered by environmental issues and the formation of non-governmental pressure groups, are already making the party rethink the way it handles public concerns. Rather than let itself run out of water, China will bite the bullet and use pricing mechanisms and penalties on polluters (both sadly inadequate now) to improve and ensure conservation. It will have no choice.

Mr Gittings hints that he was among the “sympathetic foreign observers” who admired the achievements of Mao Zedong. He is far more critical now, though he stops short of condemning Mao in the unrelenting manner of Jung Chang and Jon Halliday in their recent biography. China, he says, cannot be understood if Mao is regarded simply as a despot who was interested in nothing but power. Yet Mr Gittings's mostly dry, historical account provides few new insights into what really motivated Mao. And there is nothing on the horrors of that era that matches his vivid, first-hand account of the bloody suppression of the Tiananmen Square protests in 1989.

Reuters

Great balls of fire

The book accurately describes China's precipitate abandonment of socialism in all but name by Deng Xiaoping and his successors, and the iniquities of the unfettered capitalism that has replaced it. But it laments too much the abandonment of collectivised agriculture.

Mr Gittings believes that China's post-Mao policies have caused the “effective privatisation” of land. If only this were true. It may have caused the demise of collectivised farming, but peasants certainly do not own the tiny plots of land they work. Privatisation would give peasants collateral with which to borrow,

encourage investment in high value-added agriculture and promote urbanisation. Unfortunately the idea is still anathema to the Communist Party, which has deprived many peasants of affordable health care and education (as Mr Gittings well describes), but continues to deny them the opportunity to use their land as capital with which to make a new start in the cities. Would that it were not so.

The Changing Face of China: From Mao to Market.
By John Gittings.
Oxford University Press; 384 pages; $30 and £18.99

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18th-century heroes

Russia's Othello

Aug 18th 2005
From The Economist print edition

THIS is the life of someone who wrote little, spoke little, and about whom there are few memoirs. Yet if anyone's life is worthy of a biography it is surely Abram Petrovich Gannibal, an African slave adopted by Peter the Great, who studied mathematics and cryptography before training as a military engineer, spied for the tsar in Paris, became an expert in fortification, was sent to Siberia, became governor-general of Tallinn, and finally retired to an estate in northern Russia as the owner of slaves himself.

These days he is best known as the great-grandfather of Alexander Pushkin, whose family liked to think their illustrious forebear was an Abyssinian prince, and a direct descendant of the legendary Carthaginian general whose name he boldly adopted (spelling it in the Russian way with a "g"). It was not until the 1990s that an enterprising scholar from Benin was able to challenge centuries of Russian racism and suggest that Gannibal in fact came from black Africa.

Having travelled to Cameroon and paddled up-river in a 30-foot wooden boot to interview the Sultan of Logone, the intrepid Hugh Barnes lends credence to this theory with a tantalisingly plausible interpretation for the mysterious word "Fúmmo" (Kotoko for "homeland") to be found underneath the elephant portrayed on the family crest. Mr Barnes does far more than just "join up the dots" between Pushkin's unfinished novel about his ancestor and its subject. The result is not merely the first detailed account in English of this remarkable life, but the fullest in any language. It is a fascinating read.

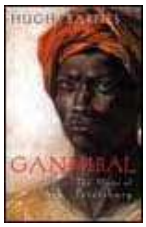
White mischief

With this book, the fruit of research in an impressive list of obscure archives, Mr Barnes not only joins the ranks of those journalists able to give academics a good run for their money, but also shows himself to be a travel writer of distinction. The story of his quest to discover Gannibal's identity in places as far-flung as Novoselenginsk on the Chinese border, and Pskov at the other end of the Russian empire, is engagingly told. With so little biographical material to go on (even the fabled portrait of Gannibal turns out to be that of a white man when it is restored), the dots have inevitably to be joined up with a degree of speculation. Just occasionally it leads the author astray—the Winter Palace, for example, was painted first yellow and then crimson before finally acquiring the "icy turquoise façade" which Mr Barnes claims greeted Gannibal when he received his dismissal from Catherine the Great in 1762.

While plenty of evidence is marshalled to show that Gannibal was the first black intellectual in Europe, his personality remains frustratingly elusive. Nevertheless, this biography of the Russian Othello does much to recast our understanding of 18th-century Russian life.

Gannibal: The Moor of Petersburg.
By Hugh Barnes.
Profile Books; 300 pages; £16.99. To be published in America by HarperCollins in June 2006

Gannibal: The Moor of Petersburg
By Hugh Barnes



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New movies

Departure lounge

Aug 18th 2005
From The Economist print edition

A sly summer satire

“RED EYE”, Wes Craven's new thriller, is a view from the ground of the daily warfare of modern life. The one-woman combat unit with whom viewers are embedded is Lisa (Rachel McAdams), manager of a Miami luxury hotel, who is flying home after burying her grandmother. As her cab races to the airport, her mobile phone rings. Her assistant Cynthia (Jayma Mays) is being verbally mauled by an older couple whose reservation is lost in the computer. No sooner has Lisa solved the problem than her divorced dad (Brian Cox) rings her up to ask for the fifth time that day if anything is wrong.

A self-described people-pleaser, the impeccably coiffed Lisa has her mettle further tested when she learns that her flight is delayed. Dante's exhortation, “Abandon all hope, you who enter”, should be written over the doors of the terminal, which is jammed with frazzled people who seem to have been there for days. Once aboard, more human sardines struggling to stow their luggage butt heads with one another and a harried flight crew. When a stony-faced stewardess can't find what she needs, she comments to a colleague: “First they take our pensions, then our coffee-pots.”

With modern air travel, Mr Craven, director of “Scream” and a master of claustrophobic horror, has found a subject tailor-made to suit his skills. By the time the plot kicks in, Lisa's discovery that her seat-mate (Cillian Murphy) is a terrorist seems the inevitable next step. He was all smarmy seduction when they met in the crowded terminal, but after a dizzying series of shifts Lisa finds instead that she has morphed into a pawn in a plot against a Homeland Security tsar staying at her hotel, with her father as the unwitting hostage of the bad guys.

Mr Craven's way with taut close-ups and unexpected twists assures audiences a white-knuckle ride, which eases just a bit when the cast finally disembarks and “Red Eye” turns into “Scream 4”. Alongside the expertly managed thriller plot lies another, more serious story, about the ongoing deterioration of our public spaces, where civility lives or dies. One sly touch: when the terrorist target first hoves into view, he is riding in an official jet. This, the film-maker seems to be saying, must be why that lunatic in steerage has it in for him—he has the whole plane to himself.

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Malian music

Notes from the Niger

Aug 18th 2005 | BAMAKO AND TIMBUKTU
From The Economist print edition

The quiet influence of Lobi Traoré

MOST Saturday nights, when he is in Mali, Lobi Traoré plays the Espace Academia club in the old airport district of Bamako. The club is like a Mississippi blues joint, minus the menace. It is about the size of a garage, with painted concrete walls, a couple of flickering light bulbs, a television over a rudimentary bar (playing French soap operas and old Paris-St Germain football matches), and an audience that includes Turkish road engineers smoking fake Dunhills, and a set of Malian girls swaying gently by a cramped stage.

Mr Traoré, squat and thoughtfully glum, arrives late in the evening, just as the crickets are stilling themselves on the dust outside. He sits at this correspondent's table, under a poster of an American rapper Tupac Shakur. Sipping pineapple juice, he fixes a stare. “So, what do you think of Jackson Browne? Cool?” Mr Traoré beams. “Yes, cool.” Such are Malian inductions into its music.

Some musicologists consider the steamy malarial swamps of the Niger river in west Africa to be the real home of the blues. Nowadays, with Air France jets streaming to Paris and beyond, the musical styles cut back and forth in Bamako. Not just the local Bambara and Songhai tunes, but soul, Congolese rumba, Cuban rhythms from socialist connections, rock (though mercifully not French rock) and latterly hip hop.

Mr Traoré has something of a hip hop look himself. His cap is slightly turned to the right, and his amulet necklace, traditional in much of Mali, is etched not with star systems or Koranic verse like those of the shepherd musicians at the edge of the Sahara, but with a bling silver guitar.

When Mr Traoré finally gets up on the stage, it is crowded with his group: bass player, another guitarist who doubles on the *ngoni*—a four-stringed lute—a rock drummer, a traditional Malian drummer and a percussionist feverishly working the calabash. Mr Traoré sings in a flat, strangely penetrating voice, somewhere between rap and blues, alternating between Malian languages. When he plays the guitar, the entire club turns to watch.

Although Mr Traoré regularly tours Europe and was recently voted “best rock artist” by *Libération*, a mainstream French newspaper, and even “best world artist” by *Le Monde*, there has been no commercial breakthrough. Instead, his work has become a valuable raw material, a kind of musical obsidian for other artists, several of whom have remixed his songs. The same is true for other Malian stars including Habib Koite, Boubacar Traoré, Amadou and Mariam, a couple who met in Bamako's school for the blind, and a Touareg group called Tinariwen. Several members of Tinariwen, whose sensibility lies somewhere between The Clash and Jimi Hendrix in the desert, were guerrilla fighters in the Touareg insurgency in northern Mali.

A Malian discography

Musician/song	Label	Year	Code
Lobi Traoré			
"The Lobi Traoré Group"	Honest Jons	2005	B0009F2CAM
"Mali Blue"	World Village	2004	B0006ZOUT
"Duga"	Oubien	1999	B00004USFR
"Ségou"	Cobalt	1996	B00000B1RQ
"Bamako"	Musicrama	1994	B00000DYJ1
"Bambara blues"	Buda	1991	B000027YL0
Ali Farka Touré and Toumani Diabaté			
"In the Heart of the Moon"	World Circuit	2005	B0009NDLJA
Amadou et Mariam			
"La Réalité"	Because Music France	2005	B0009I46VW
Tinariwen			
"Amassakoul"	Irl	2004	B0001BYL8K

Source: *The Economist*

Legend has it they went into battle with electric guitars on their backs. Mr Traoré is less martial. Born in a village on the banks of the Niger in 1963, a little way from Ségou, he did not belong to Mali's musician caste, who sing songs at weddings about kings of Timbuktu and are themselves feted as princes. The first guitar he saw, he says, belonged to a man being cured by Mr Traoré senior, a well-known healer. Young Lobi was captivated by the instrument, and he later drifted to Bamako to explore its possibilities. His breakthrough came in 1994 with his second album, called “Bamako”, which was produced by Ali Farka Touré, one of Mali's brightest stars.

Several more albums followed. The best is, arguably, the latest, called “The Lobi Traoré Group”, which was recorded in live sessions around Mali. Mr Traoré's strength on it, as with Malian musicianship in general, lies in the effortless mix of old ballads with modern riffs. “My music resembles the blues”, he says, “but it belongs to Mali.” He is modest, but not shy. “By the will of God, I will be famous,” he says. Hopefully so.

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Correction: Theodor Herzl

Aug 18th 2005
From The Economist print edition

The year when Theodor Herzl wrote about “spiriting the penniless population” across the border of Palestine “discreetly and circumspectly” was 1895 and not 1865 (“Where to now?”, August 6th).

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Economist.com PRINT EDITION OBITUARY
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Obituary

Ibrahim Ferrer

Aug 18th 2005
From The Economist print edition

Youri Lenquette

Ibrahim Ferrer Planas, a Cuban musician, died on August 6th, aged 78

NEGLECT is the essence of Cuba. Washing flaps from the balconies of what used to be thriving banks, and their once-grand elevators are caked with rust and grime. Colonial columns and cornices crumble along the back streets of Havana, and rubbish and waste water fill pits that span the roads. In elegant abandoned villas damp stains the outside walls, and mildew rots the draperies still hanging in upstairs rooms.

For years, Ibrahim Ferrer's music was treated with similar indifference. He was a band singer, fronting the orchestras that used to tour Cuba's beach resorts and casinos in the years before the 1959 revolution. When Fidel Castro came to power, those orchestras—with their evocation of Palm Court ballrooms, American tourists and capitalist *joie de vivre*—suddenly seemed unsuitable fare for hard Communist times.

The music itself, however, had always been joyously eclectic. Cuba's musicians borrowed everything, from Spanish flamenco to African drumming, from European dances to tribal litanies, to the work-songs of coffee-pickers and sugar-cane pounders. They made instruments of anything that came to hand: conch-shells, wooden boxes, metal cups. Mr Ferrer, when a child in the village of San Luis in Oriente province, played rumba with bottles and spoons at the corner of his street. He grew up to the rhythm of that, and to tango, mamba and *son*, as heard at the Social Club dances held at his grandfather's house. At one such dance, his mother had gone into labour with him. The rhythm, he liked to say, had reached him in the womb and got into his blood.

Of all these different rhythms, none pleased him so much as the *bolero*. Orphaned at 12, struggling to make his way in the world by selling peanuts in the street and singing at parties, he would hear a tango or a *son* dance number and instinctively slow it down into the lilting, romantic *bolero* style. Yet, as he complained later, he was seldom allowed to sing *boleros*. When he worked with the Chepín-Chovén orchestra and with Benny Moré in the 1950s, he was told that his voice—soft, light and pure, and as caressing as a Caribbean breeze—was too small for them. He gained his reputation improvising faster dance numbers. And then “the revolution triumphed”, in his words, and the world moved past him anyway.

For 35 years, he found other ways of earning a living. His recordings, unplayed, lay in the vaults of the Egrem state recording studios. His family was large, money short; he became a docker, a builder, a lottery-ticket seller. He shone shoes and imagined that, approaching his 70s, he would never make music again. Then, in 1996, buffing a pair of white shoes one morning outside his apartment, he was hailed by Juan de Marcos González, bandleader of the Afro-Cuban Allstars. Mr de Marcos wanted him at the Egrem studios straight away. There was no time even to wash the polish from his hands.

Mr de Marcos was taping Cuba's old music masters for a compilation. A Texan guitarist, Ry Cooder, engaged on a similar project, was listening in. Mr Ferrer—improvising, as he remembered, with his equally elderly *compadre* Rubén González on piano—launched into a racy *son* called “Candela” and then a classic *bolero*, “Dos Gardenias”. Mr Cooder, astonished, recorded both, and Mr Ferrer was shortly to become as famous a singer of *boleros* as he had ever wished to be.

The band of ancient *muchachos* Mr Cooder had assembled produced the “Buena Vista Social Club” album, which sold 4m copies and won a Grammy. There were sold-out concerts and tours. Suddenly, Cuban music swept the world. Mr Ferrer was not only the voice of it, but also the face, pictured on the sleeve of the album strolling down a Havana street in one of the golfing caps he always wore. At the tender age of 72, he went solo; he made two albums, each of which won Latin Grammys. He did not know too well what a Grammy was, only that the Americans thought him too dangerous to go to the United States in 2004 to collect it. But he was enormously, radiantly pleased.

Some of Miami's sadder Cuban exiles claimed that he was a poster-boy for Mr Castro's regime. Certainly Mr Ferrer criticised the embargo and made fun of America's stupidity at keeping him out, as well he might. He also thought Cuba a “lucky” and “strong” country. But if he was a poster-boy for anything, it was for Castroite neglect. The film that was made of the Buena Vista Social Club, itself nominated for an Oscar, showed him sitting in his tiny, decaying apartment, with a rusting refrigerator and ceiling tiles buckled by humidity, still poor. “If we Cubans cared about possessions,” he said stoically, “we should have died out long ago. But we've learned to resist.”

Inside the apartment, most of his care was lavished on a Santería shrine to Saint Lazarus. He did powerful work, Mr Ferrer believed, especially for the poor. He had two Lazarus figures of ebony, one to carry about with him and the other to be honoured with candles, honey, fresh flowers, tots of rum and meringues, if his wife had made any. Mr Ferrer would spray his Lazarus copiously with perfume, then spray himself before he went out. And it had proved lucky; like Lazarus, he too had been restored to life.

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Overview

Aug 18th 2005
From The Economist print edition

The **oil price** dropped to $63 a barrel on August 17th, easing from a recent record high of over $67.

America's annual rate of consumer-price inflation rose sharply, from 2.5% in June to 3.2% in July. However, the surge in inflation was mainly because of higher energy prices. The core inflation rate rose from 2.0% to 2.1%. Producer prices increased by 4.6% in the year to July.

Industrial output in **America** was weaker than expected, expanding by only 0.1% in July. However, residential construction was strong: housing starts in July were above an annual rate of 2m units for the fourth month in a row. In June, America ran a trade deficit in goods and services of $58.8 billion.

Consumer prices in **Britain** rose by 2.3% in the year to July, higher than the government's target of 2%. Minutes of the Bank's rate-setting committee's meeting in early August revealed that four of its nine members, including the Bank's governor, voted against cutting interest rates to 4.5%. Unemployment rose in July.

GDP in **Japan** grew at an annual rate of 1.1% in the second quarter. The economy was helped by robust household consumption and capital spending.

The **French** economy grew by a rather disappointing 1.2% in the year to the second quarter.

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Output, demand and jobs

Aug 18th 2005
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2005	2006	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 1.9	Q1	+ 2.8	+ 2.3	+ 3.1	+ 1.2	Q1	+ 1.6	Q2	5.0	Jul	5.7
Austria	+ 2.0	Q1	+ 0.8	+ 1.9	+ 2.0	+ 5.6	May	+ 3.8	May	5.1	Jul	4.9
Belgium	+ 1.4	Q2	+ 1.2	+ 1.2	+ 1.9	– 1.4	Jun	+ 4.3	May	13.4	Jul†	12.8
Britain	+ 1.7	Q2	+ 1.5	+ 2.1	+ 2.1	– 1.9	Jun	+ 1.7	Jun	4.7	Jun††	4.8
Canada	+ 3.3	Q1	+ 2.3	+ 2.7	+ 3.0	+ 1.8	May	+ 5.6	May	6.8	Jul	7.1
Denmark	+ 0.8	Q1	+ 0.6	+ 2.0	+ 2.2	+ 1.5	Jun	+ 7.6	Jun	5.8	Jun	6.5
France	+ 1.2	Q2	+ 0.4	+ 1.5	+ 1.9	– 0.4	Jun	+ 0.8	Jun	10.1	Jun	10.0
Germany	+ 0.6	Q2	nil	+ 1.1	+ 1.3	+ 2.8	Jun	+ 1.9	Jun	11.6	Jul§	10.6
Italy	+ 0.1	Q2	+ 2.8	– 0.1	+ 1.2	– 3.0	Jun	– 0.3	May	7.8	Mar	8.2
Japan	+ 1.4	Q2	+ 1.1	+ 1.7	+ 1.7	+ 0.2	Jun	+ 3.1	Jun	4.2	Jun	4.6
Netherlands	+ 1.3	Q2	+ 4.9	+ 0.4	+ 1.5	– 0.1	Jun	– 2.3	May	6.7	Jul**	6.5
Spain	+ 3.4	Q2	+ 3.6	+ 3.1	+ 2.8	– 0.2	Jun	+ 1.4	Jun	9.8	Jun	11.1
Sweden	+ 2.2	Q2	+ 2.4	+ 1.9	+ 2.6	+ 2.6	Jun	+ 9.6	Jun	7.1	Jun†	5.8
Switzerland	+ 0.8	Q1	+ 0.2	+ 0.8	+ 1.5	– 0.3	Q1	+ 3.2	Jun	3.5	Jul†	3.6
United States	+ 3.6	Q2	+ 3.4	+ 3.6	+ 3.3	+ 3.0	Jul	+ 7.6	Jun	5.0	Jul	5.5
Euro area	+ 1.2	Q2	+ 1.0	+ 1.3	+ 1.7	+ 0.1	May	+ 0.9	Jun	8.7	Jun	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 2.0	Q1	+ 0.5	na	na	– 9.8	Jun	+ 6.3	May	8.7	Jun†	8.9
Greece	+ 3.5	Q2	na	na	na	– 2.3	Jun	+ 5.3	May	9.9	Mar	10.8
Iceland	+ 2.9	Q1	na	na	na	na		na		2.1	Jun†	3.1
Ireland	+ 2.4	Q1	+ 1.0	na	na	+ 0.4	Jun	+ 4.6	May	4.3	Jul	4.4
Luxembourg	+ 3.1	Q1	na	na	na	+11.2	May	– 1.8	Jun	4.4	Jun	3.9
New Zealand	+ 1.9	Q1	+ 1.5	na	na	+ 3.5	Q4	+ 5.9	Q2	3.7	Q2	4.0
Norway	– 0.8	Q1	+ 2.2	na	na	– 2.7	Jun	+ 3.7	Jun	4.7	Jun**	4.5
Portugal	+ 0.1	Q1	+ 0.8	na	na	+ 1.2	Jun	+ 6.6	Jun	7.2	Q2†	6.3

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ‡New series. ††Apr-Jun; claimant count rate 2.8% in Jul. §EU harmonised rate 9.2% in Jun. **May-Jul.

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Prices and wages

Aug 18th 2005
From The Economist print edition

% change on year ago

	Consumer prices latest		Consumer prices year ago	The Economist poll consumer prices forecast 2005	2006	Producer prices latest		Producer prices year ago	Wages/earnings latest		Wages/earnings year ago
Australia	+ 2.5	Q2	+ 2.5	+ 2.7	+ 2.6	+ 6.9	Q2	+ 2.8	+ 4.5	Q1	+ 5.0
Austria	+ 2.2	Jul	+ 2.2	+ 2.1	+ 1.7	+ 1.1	Jul	+ 6.0	+ 2.3	Jul	+ 2.0
Belgium	+ 3.1	Jul	+ 2.4	+ 2.3	+ 1.8	+ 2.2	Jun	+ 4.2	+ 2.6	Apr	+ 2.3
Britain	+ 2.3	Jul*	+ 1.4	+ 1.9	+ 1.9	+ 3.0	Jul	+ 2.6	+ 4.2	Jun†	+ 4.2
Canada	+ 1.7	Jun	+ 2.5	+ 2.1	+ 2.2	+ 0.2	Jun	+ 7.0	+ 1.1	May	+ 3.9
Denmark	+ 2.0	Jul	+ 1.3	+ 1.5	+ 1.7	+ 4.7	Jul	+ 2.7	+ 3.1	Q1	+ 3.3
France	+ 1.7	Jul	+ 2.3	+ 1.8	+ 1.5	+ 2.9	Jun	+ 2.2	+ 2.9	Q1	+ 2.8
Germany	+ 2.0	Jul	+ 1.8	+ 1.6	+ 1.3	+ 2.5	Jul	+ 3.9	+ 0.6	May	+ 1.9
Italy	+ 2.1	Jul	+ 2.3	+ 2.1	+ 1.9	+ 3.7	Jun	+ 3.2	+ 3.0	Jun	+ 3.3
Japan	– 0.5	Jun	nil	– 0.1	+ 0.3	+ 1.5	Jul	+ 1.7	– 0.1	Jun	+ 1.8
Netherlands	+ 1.6	Jul	+ 1.1	+ 1.4	na	+ 4.9	Jun	+ 3.6	+ 0.8	Jul	+ 1.0
Spain	+ 3.3	Jul	+ 3.4	+ 3.1	+ 2.8	+ 4.4	Jun	+ 4.0	+ 2.5	Q1	+ 3.2
Sweden	+ 0.3	Jul	+ 0.7	+ 0.5	+ 1.3	+ 3.2	Jun	+ 1.5	+ 1.1	May	+ 3.1
Switzerland	+ 1.2	Jul	+ 0.9	+ 1.1	+ 1.1	+ 0.5	Jun	+ 1.5	+ 0.9	2004	+ 1.4
United States	+ 3.2	Jul	+ 3.0	+ 2.9	+ 2.6	+ 4.6	Jul	+ 4.0	+ 2.7	Jul	+ 2.0
Euro area	+ 2.2	Jul	+ 2.3	+ 2.0	+ 1.6	+ 4.3	Jun	+ 2.4	+ 3.1	Q1	+ 3.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 1.0	Jul	+ 0.3	na	na	+ 4.0	Jul	+ 1.5	+ 4.0	Q2	+ 3.8
Greece	+ 3.9	Jul	+ 2.9	na	na	+ 5.0	Jun	+ 4.8	na		na
Iceland	+ 3.7	Aug	+ 3.7	na	na	+ 3.7	Jul	+ 5.3	+ 6.3	Jun	+ 5.1
Ireland	+ 2.4	Jul	+ 2.7	na	na	– 0.3	Jun	+ 1.3	+ 6.4	Q1	+ 3.9
Luxembourg	+ 2.6	Jul	+ 2.4	na	na	+ 5.4	Jun	+ 9.2	+ 0.4	May	+ 2.4
New Zealand	+ 2.8	Q2	+ 2.4	na	na	+ 4.2	Q1	– 0.6	+ 2.5	Q1	+ 2.2
Norway	+ 1.4	Jul	+ 1.5	na	na	+19.3	Jul	+13.9	+ 3.7	Q1	+ 3.5
Portugal	+ 2.2	Jul	+ 2.8	na	na	+ 3.7	Jun	+ 2.3	– 3.0	May	+ 0.8

*RPI inflation rate 2.9% in Jul. †Apr-Jun.

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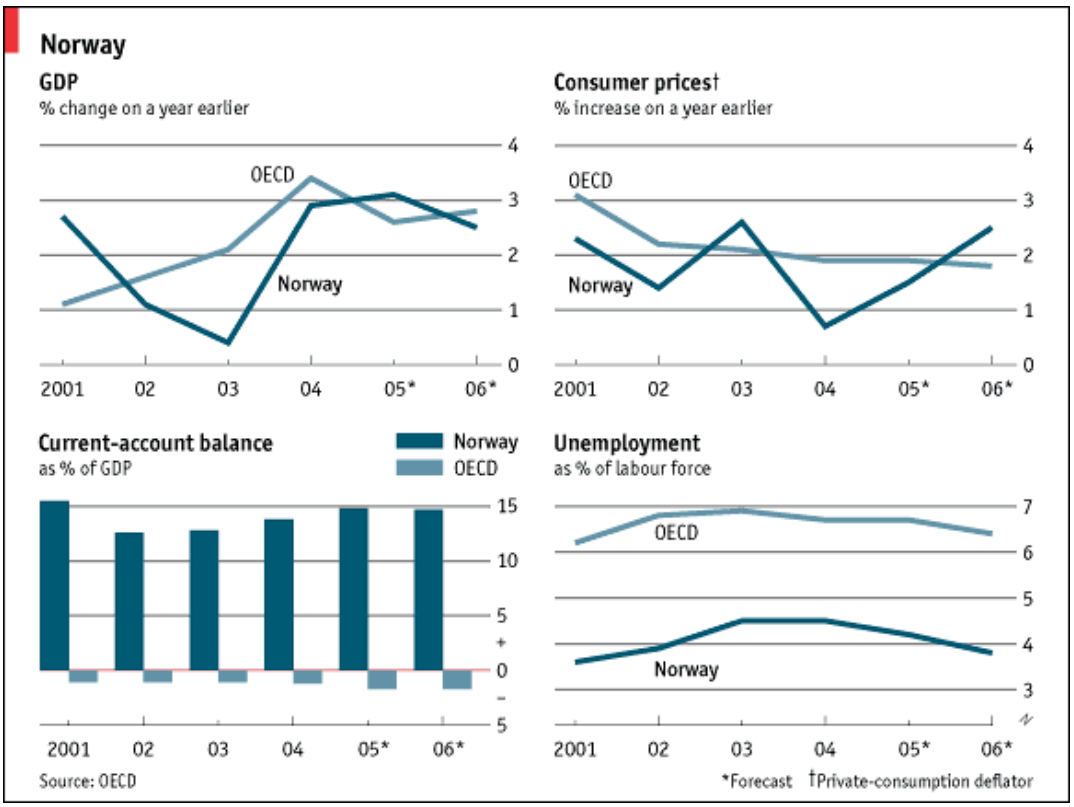
Norway

Aug 18th 2005
From The Economist print edition



After a recent dip in growth Norway is making a healthy recovery as the oil-rich economy prospers from rising oil prices. In a survey, the OECD forecasts that the economy will expand by 3.1% in 2005 and by 2.5% in 2006. Inflation, which has been subdued, will rise a bit above the OECD average. Despite the build-up of a fund financed from oil revenues, the country still faces long-term fiscal worries as an ageing population increases health and pension costs. Part of the problem, the OECD argues, arises from welfare programmes that diminish incentives to work. Although the unemployment rate is low, many Norwegians are on sick leave, drawing disability pensions or have retired early. The OECD calls for reforms that make it harder to get welfare benefits. It also recommends tightening the link between pension contributions and benefits.

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Money and interest rates

Aug 18th 2005
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Aug 17th 2005)					
				3-mth money market		2-year gov't bonds	10-year gov't bonds		corporate bonds
	narrow	broad		latest	year ago		latest	year ago	
Australia	+ 5.3	+10.6	Jun	5.62	5.42	5.03	5.17	5.58	6.19
Britain	+ 3.8	+11.0	Jun	4.53	4.91	4.22	4.28	4.95	5.19
Canada	+ 8.4	+10.4	Jun	2.66	2.05	3.14	3.96	4.68	5.33
Denmark	+21.3	+16.8	Jun	2.20	2.25	2.14	3.20	4.17	4.91
Japan	+ 4.4	+ 1.7	Jul	0.02	0.03	0.14	1.43	1.58	1.55
Sweden	+ 1.8	+ 9.4	Jun	1.47	1.98	1.98	3.12	4.32	2.86
Switzerland	+ 0.5	+ 7.3	Jul	0.76	0.52	1.03	1.94	2.63	1.94
United States	+ 1.1	+ 5.0	Jul	3.65	1.64	4.04	4.30	4.22	5.13
Euro area†	+10.5	+ 7.5	Jun	2.13	2.11	2.16	3.21	4.04	3.44

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.47%, Japan No. 270 1.43%. Central bank rates: US fed funds 3.50%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Aug 18th 2005
From The Economist print edition

2000=100

	Aug 9th	Aug 16th*	% change on one month	% change on one year
Dollar index				
All items	133.6	132.5	– 1.3	+ 7.1
Food	126.5	123.2	– 4.4	+ 4.1
Industrials				
All	142.7	144.7	+ 2.4	+10.6
Nfa†	133.2	127.2	– 6.1	– 2.5
Metals	147.9	154.2	+ 6.7	+17.7
Sterling index				
All items	113.5	111.1	– 5.2	+ 8.2
Euro index				
All items	100.0	99.4	– 4.0	+ 7.1
Yen index				
All items	138.9	134.4	– 4.5	+ 6.3
Gold				
$ per oz	433.70	444.05	+ 4.1	+10.1
West Texas Intermediate				
$ per barrel	63.10	66.12	+15.1	+41.4

* Provisional. † Non-food agriculturals.

Our commodity-price index was rebased in February 2005.

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Stockmarkets

Aug 18th 2005
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Market indices

	Aug 17th	2005 high	2005 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,429.8	4,446.3	3,905.5	+ 1.0	– 0.4	+ 9.3	+ 6.4
Austria (ATX)	3,191.3	3,260.7	2,415.0	– 2.1	– 2.1	+31.3	+18.8
Belgium (Bel 20)	3,279.3	3,314.8	2,958.8	– 1.1	–10.9	+11.8	+ 1.2
Britain (FTSE 100)	5,292.7	5,377.5	4,783.6	– 1.6	–23.6	+ 9.9	+ 3.6
Canada (Toronto Composite)	10,500.7	10,699.9	9,006.2	– 1.6	– 7.8	+13.6	+12.6
Denmark (KBX)	334.2	334.2	257.8	+ 1.2	nil	+29.6	+17.0
France (SBF 250)	3,086.8	3,146.1	2,633.6	– 1.9	–29.7	+17.2	+ 6.1
(CAC 40)	4,439.6	4,527.1	3,816.1	– 1.9	–35.9	+16.2	+ 5.2
Germany (DAX)*	4,871.5	4,990.6	4,178.1	– 2.4	–39.6	+14.5	+ 3.6
Italy (S&P/MIB)	33,495.0	34,027.0	30,645.0	– 1.6	–33.2	+ 8.4	– 1.9
Japan (Nikkei 225)	12,273.1	12,315.7	10,825.4	+ 1.4	–68.5	+ 6.8	– 0.1
(Topix)	1,250.1	1,252.1	1,109.2	+ 1.8	–56.7	+ 8.7	+ 1.7
Netherlands (AEX)	393.5	401.6	347.0	– 2.0	–43.9	+13.1	+ 2.3
Spain (Madrid SE)	1,089.0	1,103.7	950.9	– 1.3	– 5.0	+13.5	+ 2.8
Sweden (Affarsvarlden Gen)	260.3	263.6	218.9	– 1.2	–35.0	+17.7	+ 3.1
Switzerland (Swiss Market)	6,631.4	6,689.2	5,669.6	– 0.9	–21.2	+16.5	+ 5.3
United States (DJIA)	10,550.7	10,940.6	10,012.4	– 0.4	–10.0	– 2.2	– 2.2
(S&P 500)	1,220.2	1,245.0	1,137.5	– 0.7	–20.1	+ 0.7	+ 0.7
(NASDAQ Comp)	2,145.2	2,218.2	1,904.2	– 0.6	–57.5	– 1.4	– 1.4
Europe (FTSEurofirst 300)†	1,186.1	1,199.9	1,038.6	– 1.1	–30.4	+13.9	+ 3.1
Euro area (FTSE Euro 100)†	1,006.1	1,026.7	894.4	– 2.0	–35.1	+11.7	+ 1.1
World (MSCI)‡	1,196.0	1,212.0	1,115.0	– 0.6	–17.5	+ 2.3	+ 2.3
World bond market (Citigroup)††	642.2	662.3	626.9	+ 0.5	– 3.0	– 3.6	– 3.6

*Total return index. †In euro terms. ‡Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Aug 18th 2005
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Aug 17th	year ago	Currency units per $ Aug 17th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 17.7	Jun	− 42.4	Q1	− 5.9	− 5.6	117.0	110.2	1.31	1.40	2.35	1.62	1.18	+ 0.9
Austria	− 1.6	May	+ 0.5	May	− 0.3	− 0.3	103.7§	103.8	0.81	0.81	1.45	–	0.73	− 2.0
Belgium	+ 15.1	Jun	+ 12.2	Mar	+ 2.9	+ 2.8	104.1§	104.2	0.81	0.81	1.45	–	0.73	− 0.5
Britain	−111.2	Jun	− 44.0	Q1	− 2.5	− 2.6	99.7	101.1	0.55	0.55	–	0.68	0.50	− 2.9
Canada	+ 46.2	Jun	+ 20.2	Q1	+ 1.3	+ 1.2	119.4	110.2	1.21	1.31	2.18	1.50	1.10	+ 1.2
Denmark	+ 9.9	Jun	+ 10.8	Jun	+ 2.0	+ 1.8	105.8	106.1	6.05	6.05	10.9	7.50	5.48	+ 1.8
France	− 26.4	Jun	− 24.6	May	− 0.7	− 0.5	106.6§	106.8	0.81	0.81	1.45	–	0.73	− 3.0
Germany	+198.5	Jun	+108.5	Jun	+ 3.7	+ 3.5	104.3§	104.5	0.81	0.81	1.45	–	0.73	− 3.5
Italy	− 6.8	May	− 23.7	Jun	− 1.4	− 1.5	76.4§	76.5	0.81	0.81	1.45	–	0.73	− 4.4
Japan	+113.2	Jun	+166.0	Jun	+ 3.5	+ 3.4	86.8	87.1	110	110	199	137	–	− 6.1
Netherlands	+ 40.9	Jun	+ 28.3	Q2	+ 3.7	+ 3.6	103.5§	103.6	0.81	0.81	1.45	–	0.73	− 2.2
Spain	− 88.1	May	− 72.6	May	− 5.4	− 5.5	77.0§	77.1	0.81	0.81	1.45	–	0.73	+ 0.5
Sweden	+ 22.5	Jun	+ 29.7	Q1	+ 5.7	+ 5.2	96.2	97.5	7.58	7.51	13.6	9.39	6.86	+ 0.8
Switzerland	+ 7.3	Jun	+ 40.2	Q1	+11.2	+10.8	106.7	107.5	1.26	1.25	2.26	1.56	1.14	− 1.0
United States	−723.4	Jun	−717.0	Q1	− 6.3	− 6.2	84.8	86.6	–	–	1.80	1.24	0.91	− 4.1
Euro area	+ 63.5	May	+ 23.2	May	+ 0.4	+ 0.4	115.9	115.7	0.81	0.81	1.45	–	0.73	− 2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
	0.0		0.0											
Finland	+ 12.1	Jun	+ 6.0	Jun	na	na	81.2§	81.4	0.81	0.81	1.45	–	0.73	+ 1.3
Greece	− 33.7	May	− 15.5	Jun	na	na	59.7§	59.8	0.81	0.81	1.45	–	0.73	− 3.8
Iceland	− 0.9	Jun	− 1.4	Q1	na	na	105.7**	95.1	63.8	71.1	115	79.0	57.7	+ 1.1
Ireland	+ 40.9	May	− 3.1	Q1	na	na	93.6§	93.7	0.81	0.81	1.45	–	0.73	− 0.7
Luxembourg	− 4.4	May	+ 3.0	Q1	na	na	104.1§	104.2	0.81	0.81	1.45	–	0.73	− 0.8
New Zealand	− 3.5	Jun	− 7.0	Q1	na	na	136.7	130.7	1.42	1.51	2.55	1.76	1.29	+ 3.2
Norway	+ 41.2	Jul	+ 37.9	Q1	na	na	110.2	104.8	6.44	6.76	11.6	7.98	5.83	+ 14.4
Portugal	− 20.6	May	− 15.3	May	na	na	94.3**	93.3	0.81	0.81	1.45	–	0.73	− 5.3

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, June average. ‡OECD forecast. **IMF, April average.

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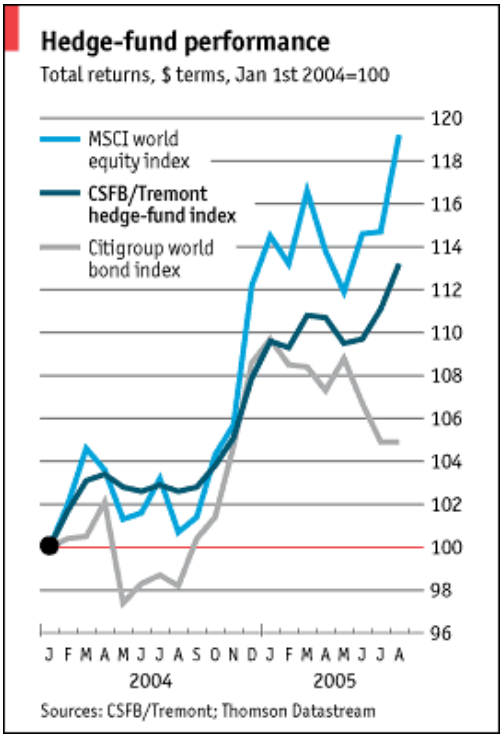
Hedge-fund performance

Aug 18th 2005
From The Economist print edition



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Overview

Aug 18th 2005
From The Economist print edition

In the year to the second quarter, GDP grew by 5.5% in **Indonesia** and by 4.8% in **Israel**. In **Peru**, growth slowed to 4.6% in the year to June.

Industrial production quickened in **Brazil**, expanding by 6.3% in the year to June, but it slowed in **Mexico**, growing by just 0.7%. Nonetheless, Mexico's GDP growth picked up a little to 3.1% in the year to the second quarter.

Russia's industrial production grew by 4.9% in the year to July. Consumer-price inflation eased slightly to 12.5% over the same period. In **Poland**, GDP grew by 2.9% in the year to the second quarter, while consumer prices rose by 1.3% in the year to July.

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The Economist poll of forecasters

Aug 18th 2005
From The Economist print edition

Every three months, *The Economist* polls a group of forecasters and averages their predictions for growth and current-account balances in 25 emerging economies. Compared with May, the panel has become more pessimistic about this year's growth outlook, lowering its projections in 13 countries while raising them in 11. However, China and India are among the countries that the panel now expects will grow a bit faster in 2005 than it did in May.

The Economist poll of forecasters

August

	Real GDP % change		Current account % of GDP	
	2005	2006	2005	2006
China	9.0	8.1	5.9	5.0
Hong Kong	4.8	4.4	10.6	9.8
India	6.8	6.9	−1.6	−1.7
Indonesia	5.6	5.5	1.0	0.6
Malaysia	5.0	5.0	12.4	11.0
Philippines	4.5	4.8	2.9	2.5
Singapore	3.5	4.7	25.0	24.4
South Korea	3.3	4.2	2.6	1.8
Taiwan	3.4	3.9	4.7	4.4
Thailand	3.9	5.0	−1.2	−1.9
Argentina	6.6	3.8	1.0	0.2
Brazil	3.0	3.6	1.4	0.6
Chile	6.0	5.1	0.7	−0.5
Colombia	3.6	3.5	−1.6	−2.2
Mexico	3.5	3.3	−1.4	−1.8
Peru	4.8	4.1	−0.2	−0.7
Venezuela	6.2	4.6	12.9	9.0
Egypt	4.4	5.2	3.8	2.4
Israel	3.8	4.1	0.3	−0.2
South Africa	4.0	4.0	−3.6	−3.5
Czech Republic	4.2	4.2	−3.6	−2.9
Hungary	3.7	3.7	−8.1	−8.1
Poland	3.6	4.4	−1.1	−1.8
Russia	5.9	5.5	10.7	7.1
Turkey	4.9	4.6	−5.1	−4.7

Sources: ABN Amro; Deutsche Bank; Economist Intelligence Unit; Goldman Sachs; HSBC; ING Financial Markets; J.P. Morgan Chase; Merrill Lynch; UBS.

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Economy

Aug 18th 2005
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.5	Q2	+16.1	Jul	+ 1.8	Jul	+87.6	Jul	+68.7	2004	711.0	Jun
Hong Kong	+ 6.0	Q1	– 0.6	Q1	+ 1.2	Jun	– 9.7	Jun	+18.5	Q1	121.9	Jul
India	+ 7.0	Q1	+11.7	Jun	+ 3.3	Jun	–32.4	Jun	– 6.4	Q1	130.1	Jul
Indonesia	+ 5.5	Q2	+10.1	Mar	+ 7.8	Jul	+27.4	Jun	+ 7.8	Q1	32.6	Jun
Malaysia	+ 5.7	Q1	+ 3.4	Jun	+ 3.0	Jul	+24.0	Jun	+16.7	Q1	74.5	Jun
Philippines	+ 4.6	Q1	+ 5.4	May	+ 7.1	Jul	– 0.1	May	+ 2.9	Mar	15.1	Jul
Singapore	+ 5.2	Q2	+11.1	Jun	– 0.2	Jun	+16.3	Jun	+32.5	Q2	116.3	Jul
South Korea	+ 3.3	Q2	+ 4.1	Jun	+ 2.5	Jul	+26.0	Jul	+23.2	Jun	204.1	Jun
Taiwan	+ 2.5	Q1	+ 1.3	Jun	+ 2.4	Jul	+ 2.1	Jul	+16.9	Q1	253.6	Jul
Thailand	+ 3.3	Q1	+ 8.8	Jun	+ 5.3	Jul	– 6.7	Jun	– 2.2	Jun	47.2	Jun
Argentina	+ 8.0	Q1	+ 2.0	Jun	+ 9.6	Jul	+11.0	Jun	+ 2.8	Q1	22.3	Jun
Brazil	+ 2.9	Q1	+ 6.3	Jun	+ 6.6	Jul	+39.9	Jul	+12.6	Jun	59.4	Jun
Chile	+ 5.7	Q1	+ 7.4	Jun	+ 3.1	Jul	+ 8.7	Jul	+ 1.1	Q1	16.2	Jul
Colombia	+ 3.6	Q1	+ 2.1	May	+ 4.9	Jul	+ 1.5	Apr	– 0.8	Q1	13.7	Jul
Mexico	+ 3.1	Q2	+ 0.7	Jun	+ 4.5	Jul	– 9.8	Jun	– 8.7	Q1	65.6	Jun
Peru	+ 4.6	Jun	+ 5.9	Jun	+ 1.4	Jul	+ 3.8	Jun	+ 0.4	Q1	14.5	Jul
Venezuela	+ 7.9	Q1	+10.4	May	+15.3	Jul	+22.6	Q1	+14.9	Q1	22.3	May
Egypt	+ 4.7	Q4	+ 3.3	2004†	+ 4.7	Jun	– 9.5	Q1	+ 4.4	Q1	17.6	Jun
Israel	+ 4.8	Q2	+ 5.2	May	+ 1.6	Jul	– 8.0	Jul	+ 1.9	Q1	24.5	Jul
South Africa	+ 4.2	Q1	+ 2.3	Jun	+ 2.8	Jun	– 2.1	Jun	– 8.5	Q1	17.2	Jul
Czech Republic	+ 4.4	Q1	+ 3.7	Jun	+ 1.7	Jul	+ 1.0	Jun	– 4.4	Q1	29.8	Jul
Hungary	+ 2.9	Q1	+ 6.5	Jun	+ 3.7	Jul	– 2.7	Q1	– 9.2	Q1	17.7	Jul
Poland	+ 2.9	Q2	+ 6.8	Jun	+ 1.3	Jul	– 3.4	Jun	– 0.2	Jun	39.8	Jun
Russia	+ 5.2	Q1	+ 4.9	Jul	+12.5	Jul	+108.6	Jun	+69.2	Q1	147.8	Jun
Turkey	+ 4.8	Q1	+ 1.6	Jun	+ 7.8	Jul	–38.3	Jun	–19.3	Jun	40.0	Jun
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+ 7.2	Q1	+11.1	Jun	+ 3.8	Jul	– 2.4	May	– 1.3	Jun	1.7	Jun
Latvia	+ 7.4	Q1	+ 9.0	Jun	+ 6.1	Jul	– 2.7	Jun	– 1.5	Jun	2.1	Jun
Lithuania	+ 8.2	Q2	na		+ 1.8	Jul	– 3.2	Jun	– 1.5	Q1	3.4	Jun
Slovakia	+ 5.1	Q2	+ 1.6	Jun	+ 2.0	Jul	– 2.0	Jun	– 2.0	Apr	15.1	Jun
Slovenia	+ 2.6	Q1	+ 1.0	Jun	+ 2.3	Jul	– 1.3	Jun	nil	Jun	7.7	May
Pakistan	+ 8.4	2005†	+13.6	Apr	+ 9.0	Jul	– 6.7	Jul	– 1.5	Q2	10.4	May
Saudi Arabia	+ 5.2	2004	na		+ 0.3	May	+84.9	2004	+51.5	2004	26.7	May

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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Financial markets

Aug 18th 2005
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Aug 17th		Dec 31st 2004	
	Aug 17th	year ago	Aug 17th	% a year		one week	in local currency	in $ terms
China	8.10	8.28	14.7	3.00	1,253.4	+2.4	– 5.8	– 3.7
Hong Kong	7.77	7.80	14.1	3.75	15,449.6	+0.7	+ 8.6	+ 8.6
India	43.5	46.3	78.7	5.47	7,859.5	+1.7	+ 19.0	+ 19.0
Indonesia	9,900	9,277	17,919	9.29	1,113.8	–5.4	+ 11.4	+ 4.4
Malaysia	3.77	3.80	6.82	2.89	926.4	–1.4	+ 2.1	+ 3.0
Philippines	55.9	55.8	101.2	7.31	1,985.1	–1.3	+ 8.9	+ 9.3
Singapore	1.66	1.71	3.00	2.00	2,280.2	–2.5	+ 10.4	+ 8.6
South Korea	1,018	1,158	1,843	3.49	1,113.3	+0.8	+ 24.3	+ 26.4
Taiwan	32.1	34.0	58.0	1.45	6,241.9	–1.8	+ 1.7	+ 0.5
Thailand	41.3	41.5	74.7	3.25	667.5	–2.5	– 0.1	– 6.0
Argentina	2.89	3.02	5.24	6.75	1,490.8	–1.2	+ 8.4	+ 11.3
Brazil	2.35	3.00	4.25	19.77	27,416.0	+1.1	+ 4.7	+ 18.4
Chile	532	636	963	3.72	9,811.5	–1.1	+ 9.5	+ 14.3
Colombia	2,306	2,611	4,174	7.01	6,993.5	+0.5	+ 60.9	+ 64.2
Mexico	10.6	11.3	19.2	9.58	14,560.3	–1.0	+ 12.7	+ 18.4
Peru	3.25	3.40	5.89	2.91	4,553.5	+1.7	+ 22.7	+ 23.7
Venezuela	2,610§	2,699§	4,723	10.50	19,009.5	+0.7	– 36.5	– 37.3
Egypt	5.77	6.19	10.45	9.40	41,384.8	–1.2	+ 68.3	+ 77.0
Israel	4.49	4.54	8.12	3.63	719.6	+2.8	+ 11.8	+ 7.6
South Africa	6.47	6.52	11.7	7.10	15,515.3	–1.4	+ 22.6	+ 6.7
Czech Republic	23.9	25.6	43.3	1.78	1,292.0	+0.5	+ 25.2	+ 17.0
Hungary	198	201	359	6.36	20,632.3	–0.4	+ 40.0	+ 27.6
Poland	3.26	3.62	5.91	4.70	30,890.7	–0.5	+ 16.0	+ 6.5
Russia	28.5	29.2	51.5	13.00	846.5‡	+3.9	+ 41.6	+ 37.8
Turkey	1.37	1.47	2.48	16.11	27,906.3	–6.0	+ 11.8	+ 9.9
EM (MSCI)*	1.00	1.00	1.81	na	615.8	–1.1	+ 13.6	+ 13.6
EMBI+†	1.00	1.00	1.81	na	349.4	+0.2	+ 6.0	+ 6.0

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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